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SEPTEMBER 19TH–25TH 2009

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Sunday September 20th 2009
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Print edition September 19th 2009

Vandalism
A protectionist move that is bad politics, bad economics, bad diplomacy and hurts America. Did we miss anything?: leader



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Politics this week

Sep 17th 2009
From The Economist print edition

The Obama administration was set to abandon a controversial **missile-defence system** that was being planned for the Czech Republic and Poland. The Czech prime minister confirmed the decision. The system, which had always rattled Russia, was proposed by George Bush citing a threat from Iran.

America raised tariffs on imports of Chinese tyres to 35%, starting a spat with China, which said it would take the issue to the World Trade Organisation. America's decision caused some to question Barack Obama's commitment to **free trade**; the tyre industry had no complaint with China's low-end products, but unions had lobbied for a steep tariff. The G20 has promised to curb protectionism. See article

After months of delay, Max Baucus, the chairman of the Senate Finance Committee, officially released his **health-care** bill, which is likely to form the basis of any eventual deal. The legislation includes a requirement for individuals to buy insurance and creates insurance "exchanges". See article

In what was described as "the largest gathering of fiscal conservatives ever", tens of thousands of **"tea party"** activists marched in Washington, where they seethed at government spending.

The House rebuked Joe Wilson, a Republican congressman, for shouting out **"You lie!"** during Mr Obama's recent health-care speech. Jimmy Carter stirred things up by suggesting Mr Wilson, and others, could not accept a black man as president, and that **racism** lay behind current conservative gripes.

New(ish) faces

Yukio Hatoyama of the Democratic Party of Japan was sworn in as Japan's prime minister, ending half a century of almost unbroken rule by the Liberal Democratic Party. He appointed Katsuya Okada, one of his predecessors as party leader, as foreign minister, and Hirohisa Fujii, a veteran bureaucrat and known fiscal hawk, as finance minister. See article

Chen Shui-bian, a former president of **Taiwan**, was sentenced to life imprisonment for crimes, including embezzlement, forgery and accepting bribes. His wife, son, daughter-in-law and several former aides have also been jailed. See article

After all the votes in last month's presidential election in **Afghanistan** had been counted, Hamid Karzai, the incumbent, had enough—55% of the total—to avoid a second-round run-off. Recounts and fraud allegations delayed an official result. See article

Ending speculation that Gloria Macapagal Arroyo may try to amend the **Philippine** constitution to allow her to serve another term as president, her party named Gilberto Teodoro as its candidate for next year's election.

A senior United Nations official, Lynn Pascoe, visited **Sri Lanka** for talks. He was expected to raise UN concerns about the slow pace at which some 300,000 internally displaced Tamils held in camps since the defeat of Tamil Tiger rebels in May are being released.

Reuters



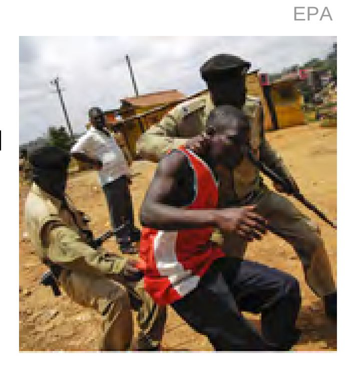
Disagreements over the script

A report to the UN's Human Rights Council on **Israel's** attack on Gaza eight months ago criticised the Palestinian movement, Hamas, but reserved its harshest condemnation for the Israelis, who rejected the document as grossly biased.

America's envoy to the Middle East, George Mitchell, continued to negotiate with Israel in the hope that it

would agree to stop building or expanding Jewish settlements in the West Bank. This would enable peace talks between the **Palestinians** and **Israel** to resume when the UN's General Assembly meets later this month.

EPA



Uganda's capital, Kampala, was rocked by days of clashes between the police and supporters of Ronald Mutebi, king of the Baganda, Uganda's largest ethnic group. At least 24 protesters were killed. See article

Helicopter-borne American special forces landed in **Somalia** and reportedly killed a suspected leader of a group tied to al-Qaeda. They took his body back to a naval ship offshore for identification. See article

Hugo builds a fortress

Hugo Chávez said that **Venezuela** would buy 92 tanks and a missile system from Russia with a $2.2 billion loan. He claims that an agreement last month under which Colombia will allow the United States access to bases for anti-drugs operations constitutes a threat to Venezuela. The United States expressed concern over an arms race in the region. See article

Brazil's economy pulled out of recession, growing by 1.9% in the second quarter compared with the first. The real rose, posting its strongest value against the dollar in a year.

Argentina's president, Cristina Fernández, who is battling a big media group, Clarín, said she would drop plans to allow telecoms companies to offer cable television. The government earlier sent 200 tax inspectors to raid Clarín.

Barroso's back

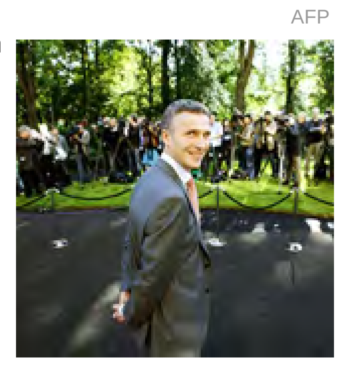
José Manuel Barroso, was re-elected as president of the **European Commission** after the European Parliament voted to give him a second term. This ended weeks of uncertainty during which Socialist, Green and Liberal critics tried to block Mr Barroso's candidacy on the grounds that he had yielded too much power to national governments and promoted the kind of free-market liberalism that led to the financial crisis.

Nicolas Sarkozy announced plans to introduce a **carbon tax in France**. It will initially be set comparatively low, €17 ($25) per tonne of CO_2 emissions, and be balanced by cuts in income and corporate tax. Heavy industry and electricity will be excluded. Socialists denounced the tax as unfair, but environmentalists said it did not go far enough. See article

Croatia will resume negotiations for membership of the European Union after Slovenia lifted the veto it had imposed because of a border dispute. The two countries agreed that no documents used in EU negotiations would prejudge the outcome of the dispute, which they will settle through international arbitration.

Russia's prime minister, Vladimir Putin, dropped a strong hint that he may formally reclaim the presidency in 2012, in "agreement" with the current holder, Dmitry Medvedev. See article

AFP



Norway's prime minister, Jens Stoltenberg, was narrowly re-elected to a second term. He is expected to push for oil exploration around the Lofoten archipelago in the Arctic, and for membership of the EU. See article

Business this week

Sep 17th 2009
From The Economist print edition

Barack Obama went to Wall Street on the first anniversary of the collapse of Lehman Brothers to tout his blueprint for overhauling America's financial regulatory system. The president recognised that the **financial industry** is "beginning to return to normalcy" after the worst panic since the 1930s, but warned that there are some "who are misreading this moment". He reiterated his administration's plans to create a Consumer Financial Protection Agency, close regulatory loopholes and hand more oversight powers to the Federal Reserve. Critics responded that the proposals would only hinder banks.



Ben Bernanke said for the first time that **America's recession** is probably over, "from a technical perspective". The chairman of the Federal Reserve cautioned that the economy's recovery would be weak initially, and job creation would be slow. In its annual report on **employment**, the OECD described the short-term outlook for jobs in the rich world as "grim".

Taking away the crutches

The **IMF** presented its guidelines for easing public aid to banks. The fund said that although it was "still too early" to withdraw substantial support, governments should be thinking hard about exit strategies and that the "recovery rates on assets acquired should be maximised". See article

It emerged that **Citigroup** has begun discussions on how to reduce the American government's 34% stake in the bank, which the Treasury bought through a preferred-stock conversion. Using Citi's current share price, the government is thought to be sitting on a paper profit of around $10 billion. Citi's share price fell sharply, however, when it sold $5 billion in government-backed bonds under emergency legislation that will expire soon, raising fears that it is still far from healthy.

A federal judge took an unusual step and set aside a proposed settlement between the **Securities and Exchange Commission** and **Bank of America** for allegedly misleading shareholders on executive bonuses paid to Merrill Lynch staff after the two banks merged. The judge said the settlement was a "cynical" agreement that did not identify precisely who was at fault, and ordered a trial. Meanwhile, New York state's attorney-general issued subpoenas to five former and current BofA directors in his investigation into the bonuses.

Morgan Stanley said that John Mack would step down in January as chief executive, a job he has held since 2005 (he will stay on as chairman). The bank's new boss will be James Gorman, who is currently in charge of asset management. See article

Robert Gates, America's defence secretary, declared that the air force would regain control of the process for awarding a $35 billion contract for new refuelling **tankers**. The air force's decision to go with an aircraft made jointly by Europe's EADS and Northrop Grumman was overturned by Mr Gates in July 2008 after auditors broadly agreed with Boeing's complaint about the procedures used to assess the project.

Circling

Japan Airlines shed 14% of its workforce, or 6,800 jobs, and reduced its schedule of international flights. It is also negotiating with other airlines keen to take a stake in JAL and gain access to its Asian routes.

The European Union's competition regulator said she would study the terms of **General Motors'** plan to spin off **Opel**, its European arm. After months of talks, GM accepted a bid from a Canadian-Russian consortium led by **Magna**, a car-parts supplier, which will invest €500m ($725m). The bid depends on

loan guarantees from the German government, which some say will lead to the protection of German jobs and the closure of more efficient plants elsewhere. See article

Adobe Systems, which is best known for its Acrobat PDF reader and Photoshop software, agreed to pay $1.8 billion for **Omniture**. With revenues falling from its graphic-design products, Adobe wanted to gain access to Omniture's technology for monitoring the performance of internet sites and web advertising.

Facebook reported that 50m people have signed up to its service since July, taking the total number of users to 300m. The social-networking website has also become cashflow positive, with enough revenue to cover its operations and capital spending. See article

Savoir vivre

Nicolas Sarkozy unveiled a report into the usefulness of **gross domestic product** as an economic indicator. The study, from a panel chaired by Joseph Stiglitz, a Nobel-prize-winning economist, was commissioned by the French president last year. It suggests that GDP could be improved by including factors that contribute towards individual well-being, such as holidays, and relying less on pure measures of market output. See article

KAL's cartoon

Sep 19th 2009
From The Economist print edition

Illustration by KAL






Barack Obama and free trade

Economic vandalism

Sep 17th 2009
From The Economist print edition

A protectionist move that is bad politics, bad economics, bad diplomacy and hurts America. Did we miss anything?



Correction to this article

YOU can be fairly sure that when a government slips an announcement out at nine o'clock on a Friday night, it is not proud of what it is doing. That is one of the only things that makes sense about Barack Obama's decision to break a commitment he, along with other G20 leaders, reaffirmed last April: to avoid protectionist measures at a time of great economic peril. In every other way the president's decision to slap a 35% tariff on imported Chinese tyres looks like a colossal blunder, confirming his critics' worst fears about the president's inability to stand up to his party's special interests and stick to the centre ground he promised to occupy in office.

This newspaper endorsed Mr Obama at last year's election (see article) in part because he had surrounded himself with enough intelligent centrists. We also said that the eventual success of his presidency would be based on two things: resuscitating the world economy; and bringing the new emerging powers into the Western order. He has now hurt both objectives.

Deeply tyresome

Last year the fear was that Mr Obama would give in to enormous protectionist pressure from Congress. By introducing the levy, Mr Obama has pandered to a single union, one that does not even represent a majority of American tyre-industry workers, and he has done so against the interests of everyone else (see article). America's tyre-makers, who have more or less given up making low-end tyres at home in favour of importing them (often from joint-ventures in guess where) declined to support the application for import "relief". Consumers will have to pay more. The motor and garage trades will be harmed. And no one can seriously imagine that any American tyre-making job will be saved; firms will simply import cheap tyres from other low-cost places like India and Brazil.

One might argue that these tariffs don't matter much. They apply, after all, only to imports worth a couple of billion dollars last year, hardly the stuff of a great trade war. China is incandescent with rage; but China is a master of theatrical overreaction. Its actual response so far has been the minor one of announcing an anti-dumping investigation into American chicken and car-parts exports. The whole affair might blow over, much as did the furore surrounding George Bush's selective steel tariffs (much worse ones than Mr Obama's on tyres) back in 2002. Presidents, after all, sometimes have to throw a bit of red meat to their supporters: Mr Obama needs to keep the unions on side to help his health-reform bill.

That view seems naive. It is not just that workers in all sorts of other industries that have suffered at the hands of Chinese competitors will now be emboldened to seek the same kind of protection from a president who has given in to the unions at the first opportunity. The tyre decision needs to be set into the context of a string of ominously protectionist policies which started within weeks of the inauguration with a nasty set of "Buy America" provisions for public-works contracts. The president watered these down a bit, but was not brave enough to veto. Next, the president stayed silent as Congress shut down a project that was meant to lead to the opening of the border to Mexican trucks, something promised in the NAFTA agreement of 1994. Besides these sins of commission sit the sins of omission: the president has done nothing at all to advance the three free-trade packages that are pending in Congress, with Colombia, Panama and South Korea, three solid American allies who deserve much better. And much more serious than that, because it affects the whole world, is his failure to put anything worthwhile on the table to help revive the moribund Doha round of trade talks. Mr Bush's tariffs, like the Reagan-era export restraints on Japanese cars and semiconductors, came from a president who was fundamentally committed to free trade. Mr Obama's, it seems, do not.

America is needed to lead. The global trading system has many enemies, but in recent times the man in the White House could be counted as its main champion. As the driver of the world's great opening, America has gained hugely in terms of power and prestige, but the extraordinary burst of growth that globalisation has triggered has also lifted hundreds of millions out of poverty over the past few decades and brought lower prices to consumers everywhere. The global recession threatens to undo some of that, as country after country is tempted to subsidise here and protect there. World trade is likely to slump by 10% in 2009, and a report from the London-based Global Trade Alert claimed this week that, on average, a G20 member has broken the no-protectionism pledge once every three days since it was made. For Mr Obama now to take up the no-protection cause at the G20's forthcoming meeting in Pittsburgh would, alas, be laughable. But if America does not set an example, no one else is likely to.

Dumb and dumber

Nor is the potential fallout from Mr Obama's wrongheaded decision limited to trade. Evidence of a weak president being pushed leftward might cause investors to worry whether he will prove similarly feeble when it comes to reining in the vast deficits he is now racking up; and that might spook the buyers of bonds that finance all those deficits. Looming large among these, of course, are the Chinese. Deteriorating trade relations between the world's number one debtor and its number one creditor are enough to keep any banker awake at night.

And America needs China for a lot more than T-bonds. Any hope of securing a climate-change agreement at Copenhagen in December on a successor treaty to Kyoto will require close co-operation between America and China. So does the work of negotiating with North Korea on its nuclear weapons. And as for Iran, where America is keen to seek a fresh round of UN sanctions in the hope of forcing it to scrap its nuclear programme, China holds a power of veto at the Security Council. Under the relevant trade laws, Mr Obama had the absolute discretion not to impose the recommended tyre tariffs on the grounds of overall economic interest or national security. Given everything that is at stake, his decision not to exercise it amounts to an act of vandalism.

Correction: the report referred to in the sixth paragraph is the work of Global Trade Alert not the World Trade Alliance. This was corrected on September 18th 2009.

The International Monetary Fund

Back from the dead

Sep 17th 2009
From The Economist print edition

But the IMF is not quite ready for the future



THE International Monetary Fund has had a good crisis. Two years ago the world's main international economic institution was heading for irrelevance, its homilies ignored by rich countries, its advice despised in poorer ones and its lending unnecessary in a world flush with private capital. Today the fund is widely hailed as a flexible and innovative crisis-responder. It has committed over $160 billion in a host of new loans and credit lines, up from barely more than $1 billion in 2007. Its lending capacity is being trebled to $750 billion.

This warp-speed revival is the result, in part, of good luck. The sudden slump in private capital flows after the collapse of Lehman Brothers a year ago was calamitous for many emerging economies, but it was a powerful reminder of the importance of an official emergency lender. Good leadership has also played a role. Dominique Strauss-Kahn, the former French finance minister who took the IMF's helm in November 2007, has shown a boldness and political deftness his predecessors lacked. His Keynesian instincts (he hails from France's Socialist Party) proved right for the times. His call for a global fiscal stimulus in January 2008, for instance, now seems prescient. He has pushed through reforms that allow the fund to dole out large amounts of money fast, while convincing a broad array of countries, including rising powers like China, India and Brazil, to contribute to its coffers (see article).

By and large this transformation should be celebrated. The world economy is better off with an IMF that has the wit and wherewithal to act fast in a crisis, and which is respected, not reviled, by its clients. If emerging economies regard the IMF as a dependable source of cash in a crisis, they might be less inclined to insure themselves against trouble by building up huge foreign-exchange reserves—as many have done over the past decade. That, in turn, would lead to more balanced global growth. Mr Strauss-Kahn, a staunch advocate of this logic, wants the fund to get much bigger, to perhaps $2 trillion.

Nonetheless, there are risks in the fund's rapid revival and Mr Strauss-Kahn's expansive vision of its future. The IMF has become relevant by lending freely, quickly and with few strings attached. But because the organisation is still dominated by rich-country governments, emerging economies are unlikely to rely on it as a lender of last resort unless there are clear rules that promise free lending in future panics. Such promises, though necessary to convince the prudent to rely on the fund, will however tempt some countries to run profligate policies. At the same time the fund still has no clout over countries it does not lend to, even if their policies hurt the global economy (as the excess build-up of reserves, especially in China, surely did). This poisonous combination could fuel instability rather than assuage it.

Move over, Belgium

Striking the right balance between being a credible lender of last resort and an effective policy policeman is hard. But it is made all the harder by the institution's governance. Rich countries, especially in Europe, wield disproportionate clout. Belgium has more votes than Brazil. China and India have paltry shares. The process of revamping countries' quotas (which determine their role in the fund) and reforming its executive board to reduce the number of Europeans has been far too slow, not least because many Europeans are fighting hard against any loss of clout. That is shamefully short-sighted. Fixing the IMF's governance and giving emerging economies more say are prerequisites if the fund is to build upon its newly acquired relevance. Those tasks should be high on the G20's agenda when it meets in Pittsburgh next week.

Goldstone on Gaza

Opportunity missed

Sep 17th 2009
From The Economist print edition

A UN report on the fighting in Gaza is deeply flawed. But that should not stop Israel holding itself and its soldiers to the highest standards

AP



TWO questions face countries that have gone to war. Was the cause just? And, where possible, did the troops do their utmost to spare civilians? It was over the second of those questions that Israel found itself under a cloud on September 15th, when a United Nations mission accused it of having deliberately committed war crimes during its three-week attack on Gaza that ended in January. Yet this week's report was deeply flawed. In a conflict where missed opportunities are as common as Qassam rockets, the risk is that both sides will now conclude the wrong thing: Arabs that Israel has just been found guilty; and Israel that it will never get a fair hearing in a hostile world.

From the very start, this report had to overcome the taint of prejudice. It was mandated by the UN Human Rights Council, an anti-Israeli outfit notorious for having congratulated Sri Lanka's government on brutal conduct that led to appalling loss of life among Tamil civilians. Israel refused co-operation. But the mission was headed by a respected international jurist, Richard Goldstone. A Jew himself, Mr Goldstone insisted on scrutinising the conduct of Hamas as well as Israel. There was hope that he might wrestle the inquiry into balance.

Yet the report takes the very thing it is investigating as its central organising premise. Israeli policy in Gaza, it argues, was deliberately and systematically to inflict suffering on civilians, rather than Hamas fighters (see article). Israel's assertions that, in the difficult circumstances of densely populated Gaza, it planned its military operations carefully and with constant legal advice are taken by the report as evidence not of a concern to uphold international law but of a culpable determination to flout it. Israel's attempts to drop warning leaflets, direct civilians out of danger zones and call daily humanitarian pauses may well have been inadequate, but the report counts them for nought. As many as 1,400 people died in the fighting. It is a grisly thought, but if Israel really had wanted to make Palestinian civilians suffer, the toll could have been vastly higher.

Israel has argued that Hamas fighters endangered civilians by basing themselves around schools, mosques and hospitals. The mission had Hamas's co-operation, but its fact-finders could detect little or no evidence for this—despite plenty of reports in the public domain to support it. The report does criticise Hamas for firing rockets indiscriminately into Israel and for using the conflict as cover to settle scores with its Palestinian rivals. But its seemingly wilful blindness to other evidence makes that look like a dash for political cover.

To some, Israel's Gaza war will always be in principle unjust: a disproportionate response to Hamas's rockets. Indeed, the suffering in Gaza, from war and the economic blockade, has been grievous. They may be tempted to applaud Mr Goldstone's report for that reason alone. Yet if the mere fact of Israel's attack were enough to condemn it then Mr Goldstone's report was pointless all along. And there is a danger of

double standards. American and European forces in Iraq, Afghanistan and Kosovo also caused thousands of civilian deaths, without attracting a Goldstone.

Eyeless in Gaza

The pity is that the report frustrates the objective that Israel should be striving for: to hold its politicians and soldiers to the highest standards of Israeli and international law. After its costly war in Lebanon in 2006, Israel plainly chose to minimise its own casualties by using massive firepower in Gaza. It went too far. There have been credible allegations that individual soldiers broke rules banning the use of Palestinian civilians as human shields sent first into properties where fighters may be holed up; that civilians known not to pose any military threat were killed in cold blood and that Israeli forces used white phosphorous over built-up areas. Israel is pursuing 23 criminal investigations so far into the Gaza operations. It must finish the job. Unlike Syria, say, Israel is a democracy that claims to live by the rule of law. It needs to make its case by moral force as well as by force of arms.

The UN report has not come at a good moment. Barack Obama is trying to restart direct talks between the Palestinian Authority and Israel. The peace process was never going to be easy. With its thimbleful of poison, the Goldstone report has made the job all the harder.

Tobin taxes

The wrong tool for the job

Sep 17th 2009
From The Economist print edition

A global tax on financial transactions would make it harder to deal with troublesome banks

Bloomberg



"IT IS usually agreed that casinos should, in the public interest, be inaccessible and expensive. And perhaps the same is true of stock exchanges." John Maynard Keynes, writing in the 1930s, was in favour of making it costly to switch into and out of investments. With just a trace of English snobbery, he wrote approvingly of the high fees and taxes levied on share transfers in the City of London, which he contrasted with the lower turnover costs on Wall Street. The smooth workings of New York's stockmarket served only to promote "speculation" over "enterprise", he wrote. The sins of London were less grave.

Three generations on, public disgust with "casino capitalism" and the return of fat profits and bonuses in an industry so recently rescued from oblivion have led to new demands for a levy on securities trading. In the run-up to Germany's general election, the Social Democratic Party has called for a global tax on financial transactions to curb the excesses of finance and to help cover the fiscal costs incurred by the banking crisis. And Adair Turner, the head of Britain's banking watchdog, the Financial Services Authority, has said that a turnover tax might be considered if capital rules to make banks bear the full costs of risky trading cannot be made to work.

James Tobin, a Nobel-prize-winning economist and disciple of Keynes, first proposed the idea of a global transactions tax—on foreign exchange—in 1972. This newspaper has regularly criticised it on two counts: it would be unworkable unless all governments signed up to it (and perhaps even if they did); and a levy would harm the liquidity of financial markets, making asset prices more volatile. Now there is a third, equally valid objection: that a Tobin tax is a poor solution to the problems in banking—too much leverage, too little care taken in assessing risks and banks that are deemed too big to fail.

Actually, we've tried this already

Though they are often presented as a radical measure, Tobin-style levies on capital transactions are in fact widespread. The stamp duties paid on British share purchases in Keynes's time survive to this day, though they are easily sidestepped by investors using derivatives. Home sales also attract a turnover tax in Britain and elsewhere. In America investors pay a tiny fee on asset transactions to cover regulatory costs. In principle such levies are useful if they meet the test for taxes: to raise revenue without harming price signals and enterprise too much.

But Tobin taxes measure up badly against that benchmark. They are often easy to avoid, so yield thin revenues. Sweden's experiment with hefty levies on share, bond and derivative trades in the 1980s was

abandoned in 1991, after it led to a sharp drop in trading volumes. Swedish investors escaped the tax by placing orders abroad. Even if that fate could be avoided by introducing a harmonised global tax—and there are more pressing claims on international co-operation, such as the regulation of cross-border banks and capital rules—investors would find ways to bet on markets that side-stepped the levy.

What of the effect on liquidity? Academic research suggests that higher turnover costs lead to more volatile markets and to distorted price signals. The harm done to liquidity in capital markets by turnover taxes may seem abstract when the banks' fortunes are reviving so immodestly. But the more that borrowers can meet lenders directly in free-flowing markets, the less dependent they are on brittle banks for credit. Keynes disliked the "fetish of liquidity" but accepted that it was necessary to persuade investors to take risks.

Another problem is that taxes on transactions could drive derivative trades off exchanges, just as regulators are trying to encourage them on. Indeed, suspicious souls may even wonder whether the banking lobby is behind the clamour for a turnover tax, since it gives credence to the idea that low-cost trades are bad, and so indirectly justifies the high fees that banks charge for bespoke derivatives. Taxes on capital markets' turnover could even strengthen the privileged position of big banks in the financial system.

Most importantly, a Tobin tax would be a poor way to address finance's biggest sins, because trading volume is a poor guide to the size, risk-taking or complexity of banks. It would punish high-frequency trading, but this was peripheral to the crisis. (Such strategies are often used to hedge risk rather than increase it—and where they are not, the costs are borne more by investors than banks.) Nor would a Tobin tax prevent bubbles. The irony that the roots of the crisis lie in housing markets, where turnover costs are high, is often lost on the tax's proponents. Investors keen to buy into markets where prices have already risen are not deterred by a small levy. Finance needs fixing, but a Tobin tax is the wrong tool for the job.

The car industry

Trouble down the road

Sep 17th 2009
From The Economist print edition

Carmakers are recovering after a terrible year. But daunting long-term problems remain

Illustration by Peter Schrank



LAST December the boss of Fiat, Sergio Marchionne, predicted that the economic crisis would finally force the world's car industry to confront profit-destroying overcapacity and change its broken business model. He also thought that, by the end of 2010, consolidation would result in there being only six high-volume carmakers left in the world. This week, as the industry gathered in Frankfurt, he returned to his theme. But his predictions look increasingly like wishful thinking.

Across the world governments have lavished their ailing car firms with subsidies. Although General Motors (supported with over $50 billion of taxpayers' money) has shed some brands and factories in America, so far not a single carmaker of any size has disappeared. One of the weakest was Chrysler, but thanks to a $7 billion federal bail-out and a deal with none other than Fiat, it motors on. So too does GM's perennially lossmaking former European arm, Opel/Vauxhall, propelled with a €4.5 billion ($6.5 billion) dowry from the German government last week into the arms of Magna, a Canadian auto-parts company, and Russia's Sberbank.

Opel's new owners are threatening to cut some jobs and, perhaps, shut a couple of small factories in Belgium and Britain. But the remarkable thing is that not a single car factory in Europe has closed in the past 12 months. According to industry estimates, overcapacity in Europe next year will be around 7m units, or 30%. In America, a market of similar size, overcapacity will fall from about 6m vehicles this year to 3.5m next year, but a great deal of the overcapacity elsewhere will be aimed at America when sales begin to recover. There is no chance of the gap being filled by rising demand in rich countries: carmakers agree that nearly all their future growth will come from emerging markets, such as China, Brazil and India.

Overcapacity is not the only structural problem confronting the carmakers. The other, potentially just as damaging to profits, is a shift toward smaller and more fuel-efficient cars (see article), caused by three factors. First, cheap credit, especially lease finance, and home-equity withdrawal let people buy more expensive cars in recent years. Without such easy money, they will trade down to smaller models. Second, demographic shifts in rich countries favour smaller vehicles: older people tend not to buy large, powerful cars, which is particularly bad news for Germany's premium carmakers. Third, as governments try to meet their carbon-reduction targets they are tightening emissions standards and penalising vehicles with big engines.

The problem with small cars, from the industry's perspective, is that they are much less profitable. Many carmakers actually lose money on their small cars, but plug the gap with profits from larger models. As the mix shifts towards smaller models and carmakers have to devote more research spending to

developing greener vehicles, profits will suffer. Compounding these long-term worries is the industry’s dependence on scrappage schemes, which have boosted demand this year, especially in Europe. Many, if not most, of the sales prompted by government incentives for people to scrap their old cars were to people who would not otherwise have bought a new car. But some were to people who brought purchases forward in order to benefit from the schemes. Just how much this will affect future demand remains unclear.

Put your foot down

All this means that the industry’s return to health is by no means assured. Government aid, in the form of bail-outs and scrappage schemes, may have prevented outright collapse, but it has merely delayed the reckoning. Rather than waiting for the crisis to strike once again, the inevitable restructuring will be less painful if it is done during an upswing. The industry needs to get smaller while finding a profitable way to make small, green cars. Mr Marchionne’s predictions that the car business will have to close factories to reduce overcapacity on the one hand, and consolidate into a smaller number of big firms to cut costs on the other, may not come true next year. But one way or another, they will come true eventually.

Set Angela free

Sep 17th 2009
From The Economist print edition

Voters should release Angela Merkel from the cage of Germany's grand coalition



IT HAS Europe's biggest economy and is its most important country. But you may be forgiven if you have failed to notice that Germany is holding a general election on September 27th. The campaign culminated on September 13th in a turgid televised duel (swiftly branded "a duet") between the two main candidates for chancellor, Angela Merkel and Frank-Walter Steinmeier. It has all been deeply uninspiring.

That is in large part because it has long been obvious that Ms Merkel will win again. The only (apparently minor) issue has been whether she can form a new coalition between her centre-right Christian Democrats (CDU) and the liberal Free Democrats (FDP), led by Guido Westerwelle; or is reluctantly obliged to prolong today's "grand coalition" with Mr Steinmeier's Social Democrats (SPD). At present the second of these looks more likely. That should worry Germany.

The grand coalition was imposed on Ms Merkel after the 2005 election, when the CDU did less well and the SPD rather better than most pollsters had predicted. Many critics were mindful of a previous unhappy grand coalition between 1966 and 1969, but this one has proved more durable than they feared. Ms Merkel has shown herself to be a capable and pragmatic political leader, and she has remained popular with voters, despite Germany's worst recession since the war. The coalition has even taken a few brave decisions, such as pension reform and sending extra troops to Afghanistan.

Yet as so often in a forced marriage of opposites, the government has been unable or unwilling to tackle many other pressing problems, such as tax, health care, welfare and labour-market reform. Too often, the view within the coalition has been that big changes in these areas are too tricky to make or even discuss—so they are best put off to another day. In this, the politicians display not only their own timidity but also the mood of many voters. Especially as the economy has started to recover, Germans seem to believe that all that is needed are a few minor repairs to the public finances, a renewed emphasis on cost control and a prayer that unemployment does not rise too far. If so, they think, they can just sit back and wait for another global boom to revive the great German export machine.

Wanted: more angst

This is profoundly mistaken—and dangerously complacent, even in the short run. Germany's banks, which dabbled extensively in toxic assets in America and elsewhere, look a lot sicker than their bosses (or their regulators) have so far admitted. Unemployment, which has been held down before the election by wage

subsidies and make-work schemes, is sure to rise soon after the polling stations close. The world economy is certainly improving, but growth is unlikely to be fast enough to save Germany from its problems—and there is a risk that the economy could tip back into recession again.

Far worse, the complacency of voters and politicians alike ignores almost entirely Germany's serious medium- and long-term difficulties. As our briefing sets out, the country's grim demographic outlook could bust the budget; too much regulation and an excessively generous welfare state together hold back job creation and inhibit entrepreneurship; the education system no longer serves secondary-school children or university students well; and there is a pressing need to reorient the economy away from high savings and a reliance on exports and towards higher consumption and the industries that cater to it.

None of these is easy to deal with. But a fresh Merkel government is far more likely to make the attempt if it takes the form of a CDU-FDP (black-yellow) coalition than if it is another grand coalition. It would also improve German foreign policy, even though this has not been much of an issue in the campaign. As foreign minister, Mr Steinmeier has proved soft on Russia, and his party is turning against the war in Afghanistan. A black-yellow coalition, in which Mr Westerwelle might be foreign minister instead, would be a bit tougher: the FDP is not only the most pro-business of the parties but also the most pro-American. It has also been the boldest in suggesting tax and welfare reforms. For all these reasons, if this newspaper had a vote in Germany's election, it would cast it for the FDP, in the hope that it joins a coalition with Ms Merkel's CDU.

Left in opposition

There are more profound arguments against a repeat of the grand coalition. The polls suggest that German voters have turned against the SPD, which has been in government for 11 years and is likely this time round to register its lowest vote in half a century. The party would benefit from a spell in opposition, where it can debate and, with luck, come to terms with the case for further reform and yet at the same time find a way to win back support from the rising Left party. It needs new leadership to balance these apparently conflicting tasks. If the SPD limped on in government, that would not just strengthen the appeal of the Left but be a travesty of voters' wishes.

The perpetuation of a grand coalition also runs into broader objections. Yoking together Germany's two *Volksparteien* in one government tends to stifle the coherent, mainstream opposition that is essential to the cut-and-thrust of policymaking in any democracy. Deprived of choice, disgruntled voters tend to drift towards extremism or apathy, thereby weakening the big parties even more. Indeed, there is a growing risk that, with five parties always likely to win seats in the German parliament, it may become all but impossible to have anything other than a grand coalition. What ought to be an emergency arrangement might turn into a permanent one. That would not be good for democracy.

Germans are fond of consensus. Both Ms Merkel and her grand coalition reflect this. Although she briefly espoused radical reforms in the 2005 campaign, she soon dropped them and, as chancellor, she has proved cautious and methodical. The hope is that it is less her own nature that has stopped her from putting the case for more reform, than her imprisonment with her SPD partners. It is time to set Angela free to see what she can do.



On electric cars, Vladimir Putin, antitrust policy, Canada, Cisco Systems, Congress, meetings, Richard Dawkins

Sep 17th 2009
From The Economist print edition

A levy on the Chevy

SIR – One factor that currently makes electric cars cheaper to drive, and which was not raised in your briefing on the electrification of motoring, is that there are not yet any significant taxes on the electricity used to charge the vehicles ("The electric-fuel-trade acid test", September 5th). Indeed, governments subsidise consumers to encourage them to buy hybrid cars. But if there is a marked shift away from petrol-based motoring, governments will lose vast sums of tax revenue that are now paid at the pump. They will need to replace this income somehow, and my bet is they will introduce a tax on the electricity used to charge cars such as the new Chevrolet Volt, a mileage tax or some other tax not yet invented.

Leonard Surette
Santa Ynez, California

SIR – Has anyone thought about where we will get the lithium for the batteries that power electric cars? Although lithium is relatively abundant the largest reserves are found in Bolivia, and Russia has sizeable deposits. We should give the issue more consideration before we swap a dependence on oil for a lithium cartel led by Hugo Chávez's friends.

Norman Hardie
Toronto

Russia's prime minister

SIR – Far from being "evasive" about the Molotov-Ribbentrop pact, Vladimir Putin was unequivocal ("The unhistory man", September 5th). He said that "any kind of collusion with the Nazi regime was morally unacceptable and had no prospects of practical implementation." He also pointed out, quite fairly, that a whole host of mistakes were made by many countries in the run up to the war.

But the message that Mr Putin took to Gdansk was to a lesser degree about history. Rather, he spoke about the future and expressed his wish that the "shadows of the past should no longer cloud" relations between Poland and Russia. Mr Putin said we must draw lessons from history, but that "exploiting memory, anatomising history and seeking pretexts for mutual complaints and resentment causes a lot of harm and proves lack of responsibility."

Again, I do not think he could have been clearer.

Dmitry Peskov
Spokesman for the Russian prime minister
Moscow

Big doesn't mean bad

SIR – Your article on antitrust policy in America was premised on a misunderstanding of the core principles of the law ("Return of the trustbusters", August 29th). Antitrust law does not forbid a company from becoming too successful. It instead prohibits a business from becoming a monopoly through using practices for the purpose of suppressing current and potential competition. The fundamental distinction is simple. A successful company tends to eclipse its rivals because those rivals cannot match its superior methods. Anti-competitive businesses, by contrast, employ abusive, destructive practices in order to impair meaningful competition across entire markets.

America's antitrust laws assume that competition will keep sellers honest and on their toes. During the Bush administration officials were almost openly contemptuous of these principles. They practically championed the cause of dominant, stultifying firms, and they infamously gutted the Microsoft case after the preceding administration had won it.

You seemed to be fixated with knocking down a straw man—the big-company-is-bad thesis. That is why you failed to grasp how terribly the Bush administration conducted itself in matters of antitrust law. In America we do not have a reflexive distrust of big, successful companies, only of corrupt, oppressive ones.

William Markham
San Diego

Harper's realm

SIR – The "assertion of sovereignty" is irrelevant to Canada's policy on the Arctic ("Harper of the melting North", August 29th). Most Canadians, however, have swallowed jingoistic nonsense from the government about a supposed need to affirm the country's "sovereignty" in the region (Stephen Harper said we should "use it or lose it"). There is simply no threat. No foreign country makes any claim to the territory, the Danish claim to tiny Hans Island aside. There is in reality as much need to assert our sovereignty through an increased military and governmental presence in the north as there is in, say, Newfoundland.

What is in dispute is Canada's claim that the Northwest Passage is Canadian "internal waters", a claim that almost nobody else accepts, including the United States, the European Union and Japan. But that is strictly a separate legal maritime issue. Areas of the Arctic seabed are also in contention, though there can be no threat to a sovereignty that has, in this case, not yet even been asserted.

Mark Collins
Ottawa

The Cisco way

* SIR – Your briefing on Cisco Systems did a masterful job of capturing the scope and rationale for the company's expansion into adjacent markets ("The world according to Chambers", August 29th). I would, however, like to clarify one point, since the article attributed to me a concern about management stress posing a downside risk of this effort. I do indeed believe that is a risk, but I unequivocally support both the scope of Cisco's ambitions and the council and board management system it has put in place to meet them. Here's why.

The internet in each of its dimensions is re-engineering life on our planet. This creates opportunities for Cisco to reposition itself from plumbing to platform. In the technology sector, markets organise around platform providers, locking them in—and their competitors out—for decades. It is critical that Cisco throw its hat into every one of these rings before they close up, hence the scope of its expansion.

Large corporations have traditionally failed to capitalise upon such disruptive opportunities because they cannot easily focus their resources across functions to create new markets. This role has fallen to venture capital. Drawing on these lessons, Cisco's collaborative management system simulates the entrepreneurial-team dynamics of a venture-backed start-up, creating a fluid structure that does not get locked up in the operating dynamics of a multi-billion-dollar enterprise.

You correctly cited Cisco's telepresence capabilities as a critical enabling technology for collaborative management. But neither it, nor anything else I have read on the subject, comes close to capturing the impact this technology has had on decision-making inside the company. When you can bring people together at any hour of the day or night for life-size, face-to-face discussions that are as good as being there (better, really, since no private jet is as good as sleeping in your own bed), you can act at a scale and speed that has been previously unimaginable. Executive engagement at Cisco has become qualitatively different from any other organisation I have ever worked with, and I fully expect this style to become the norm for global enterprises.

One final point, because it is the obverse of my previously expressed concern about the inevitable stress and strain of converting to a collaborative management system and the toll it might take on people in the midst of that learning curve. For high-potential executives—the heart and soul of any workforce—Cisco is

simply an amazing place to work, not because it is easy, but because it gives them unprecedented visibility and impact at the highest levels of the corporation. How often do you get to shape the world?

While most global chief executives are struggling to imagine how, given the law of large numbers, they will ever be able to generate more than low single-digit growth, John Chambers is riding a wave of opportunity that towers over such outcomes.

Geoffrey Moore
San Bruno, California

Past and present

SIR – Your report on Congress's bickering parties stated that "America harks back to those bipartisan idylls of yore" ("Why can't they just get on?", September 5th). Bipartisan co-operation, on health care at least, has always been rare. Lyndon Johnson just about got enough southern Democrats on board for Medicare to pass. Those same southern states are now in the hands of southern Republicans, who remain dead-set against any government involvement in health care. Nothing much has changed, except that conservative ideology is deeper and more entrenched than ever, virtually eliminating any opportunity for bipartisanship on any subject.

Ronald Schaeffer
Lewes, Delaware

Company sclerosis

SIR – It was sad to read that BT is "battling decline"("Friends, family and grandads too", August 22nd). I have had many commercial dealings with the company and I think one factor that contributed towards its weakness is that it still acted like a state-owned firm. BT's representatives were always coming from a "meeting about this meeting" and usually after our meeting had finished they were off to another meeting. Managers from two or three divisions would have to give their approval before anything was "actioned".

Richard Francis
Bracknell, Berkshire

Unintended consequences

SIR – When it comes to evolution, Richard Dawkins certainly excels at preaching to the choir of which your reviewer is evidently a member ("It's all there", September 5th). But it is not obvious that he successfully communicates science to the general public: the understanding of evolution has not exactly increased during his career. Rather, his sometimes strident and intolerant tone, and apparent bundling of evolution and atheism, may have been quite effective at promoting creationism.

Patrick Gilligan
Singapore

SIR – You posited that trees would be better served by remaining small, and wryly submitted that "surely an intelligent designer would have put the rainforest canopy somewhat lower, and saved on tree trunks?" But if all trees were to remain short, perhaps you could explain what giraffes, with their over-sized necks, would be able to eat?

Brett Hannigan
Philadelphia

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* Letter appears online only



Germany's election

A change of partners?

Sep 17th 2009 | BERLIN AND SAARBRÜCKEN
From The Economist print edition

Angela Merkel would like to head a new coalition. That would be just the start to answering Germany's long-term problems

AP



SAARLAND, the smallest German state without the excuse of being just a city, is a thumbnail caricature of Germany. It was here, among the woods and hills, that Goethe in 1770 claimed to discover that "passion for reflection on economic and technical matters" that occupied much of his life. For decades the thick coal seams underneath it made Saarland a pawn in the power-games of Germany and France. And because of that history, the sort of industry that Germany is known for—cars, steel and machines—looms even larger in its economy than in the rest of the country.

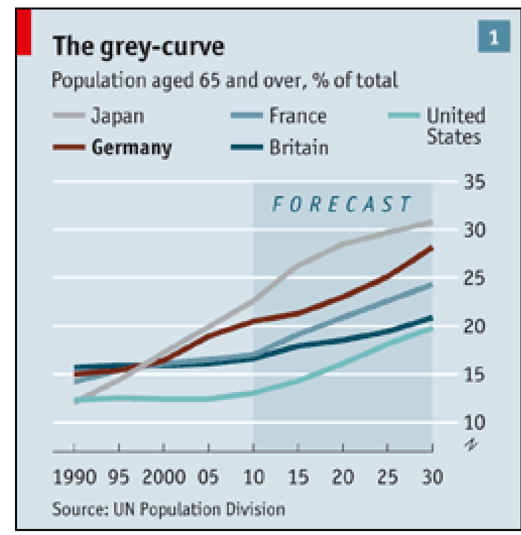
After 2000 that was a blessing. Orders poured in, and Saarland—though once a bit of a joke to Germans in the *Reich*, the locals' rueful name for the rest of the country—outpaced Germany's growth. Though the coal was becoming too costly to mine, Saarland upgraded old industries like steel and ventured into new fields, such as information technology. But when the global financial crisis broke, hitting Germany's export-dependent economy harder than most, the self-described "rising state" tumbled even further. Like the rest of Germany, Saarland is now praying that the recovery will be sufficiently swift and strong to stave off mass unemployment.

The crisis and its aftermath have provided unsettled political weather for Germany's federal election, to be held on September 27th. The chancellor, Angela Merkel, who is running for re-election, promises to lead Germany "cleverly out of the crisis". Her main challenger, Frank-Walter Steinmeier, the foreign minister, is trailing largely because voters doubt he would be any smarter in this respect. In surveys of voters' opinions about the economic competence of the two biggest parties, Ms Merkel's Christian Democratic Union (CDU) handily trumps Mr Steinmeier's Social Democratic Party (SPD).

But a second glance at Saarland tells you that crisis-management is not all that matters. Saarlanders are older than other Germans; despite its economic success, the state's tiny population of 1m is shrinking through a falling birth rate, mortality and emigration. The rest of Germany is not far behind. It is among the world's fastest-ageing countries (see chart 1). This year western Germany will pass a demographic milestone: the number of people of working age will shrink for the first time, as has already happened in the formerly communist east. Politicians have had little to say about this in their quest for Bundestag seats. In Saarland, for example, the hottest issue seems to be whether towns, to save money, may have to close their swimming pools. But the consequences of an ageing population will be longer-lasting than those of the economic crisis and at least as far-reaching. So Saarland's towns are wondering whether it is worth spending money on swimming pools when the number of children is falling. The greying of Germany raises the stakes for almost everything the next government will do.

This is not what Germans call a *Richtungswahl* (turning-point

election). Unlike the Americans or the Japanese, they are not pining for change. Germany profited handsomely from booming world trade, creating 1.6m jobs between 2005 and 2008. When the crisis hit, the government deflected the pain, at least until after the election. Ms Merkel and Mr Steinmeier—both exuding sobriety and competence, but hardly setting passions alight—have governed together in a "grand coalition" for the past four years, which gives their contest the feel of sibling rivalry. Relieved they have not suffered more, Germans seem ready to give Ms Merkel a second term without inquiring too insistently how she might use it.



Yet the election will not be a coronation. The main choice voters face is whether to extend Ms Merkel's cranky partnership with the SPD or to heed her plea for a change of coalition: she would rather govern with the smaller Free Democratic Party (FDP). That would not be a trivial change. The SPD and FDP stand almost at opposite poles of Germany's political spectrum. The SPD preaches "solidarity", which entails strong worker protection, minimum wages and robust social welfare. The FDP champions "freedom", which goes along with sharply lower taxes, less regulation and friendliness to private enterprise. Ms Merkel 's CDU and its Bavarian sister party, the Christian Social Union, stand uneasily in the middle. All four accept the tenets of Germany's "social market economy". Both the Social Democrats and the Liberals have mellowed, which means that the next government is unlikely to bring in radical change, no matter what its makeup. But a government with liberal leanings is more likely to keep Germany vigorous as it ages, and is what Ms Merkel says she wants.

Voters do not share her tastes. Less than a third favour a "black-yellow" partnership of the CDU and the FDP. With the crisis easing, voters are paying more attention to the SPD's solidarity agenda. Mr Steinmeier outscored Ms Merkel in their only televised debate (a muted affair, to which the opposition was not invited), mostly by coming across for the first time as someone who could do her job. But he has little chance of winning outright, and virtually none of forming a left-wing coalition in the Bundestag. Hence the possibility of another grand coalition.

Lucky for some

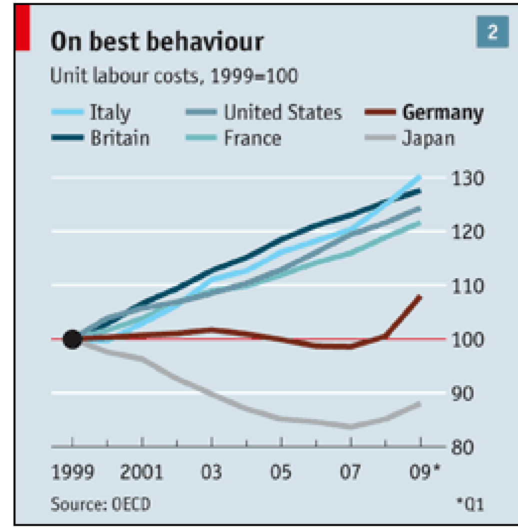
The muddy political choices reflect the murky mood of the electorate. On the eve of the election Germany deems itself a successful country, lucky to have escaped the worst of the recession. It is among Europe's most competitive economies and second only to China as an exporter of goods. But the fruits of success seem to be distributed unevenly. Relative poverty and inequality have risen faster in Germany than in any other OECD country since 2000, says Gustav Horn of IMK, a union-linked think-tank. And since 1999 Germans' wages have risen less than anywhere else in the euro zone. Even before the recession Germans were grumbling about the pay of corporate fat cats. Now executive pay sometimes seems to be the most emotive campaign issue.

These discontents are reverberations from German unification in 1990, which saddled the country with gargantuan costs and led to a decade-long quest to regain competitiveness. The private sector did much of the work: enterprises restructured and trade unions accepted low pay rises and more flexible contracts. The grand coalition's predecessor, a left-leaning partnership between the SPD and the Greens, enacted tough reforms of the labour market, including "Agenda 2010", which chopped unemployment benefits. Ms Merkel's government topped that up by raising the pension age (gradually, from 65 to 67, starting in 2012), cutting corporate tax rates and almost balancing the federal budget before the crisis knocked it askew.

The reforms pushed more people into work and reduced the price of labour (see chart 2), which helped firms take full advantage of the boom in world trade. Long-term unemployment dropped by 40% in 2007 and 2008, the first big retreat in absolute numbers since the 1960s, notes Joachim Möller, director of IAB, the federal employment agency's research unit. Most Germans credit the government's anti-recession measures, such as "cash for clunkers" and subsidies for firms to hold on to workers, for the fact that unemployment has risen only mildly so far. In fact, this "German miracle" may owe as much, if not more, to Agenda 2010.

But Germans are tired. Sure, Saarland created lots of jobs during the boom years, says Eugen Roth, head of the trade union confederation in the state and an SPD official. But too many of

these were the insecure, low-paid positions encouraged by the reforms. In Saarlouis, for example, Ford is employing temporary workers alongside assembly-line veterans; in a crisis, they will be first to go. A chastened SPD has been trying to make amends. The grand coalition extended unemployment benefits for older workers, and broke a contract between generations by promising the retired that their pensions would never fall. Such reversals scare economists, many of whom say their priority for the new government is that it do no more harm.



But that will not be enough. The next government will have to fend off the credit crunch and redesign the regulation of banks, which may be in worse shape than officials have yet let on. Germany can no longer count on exports alone to turbocharge its economy, but it is not clear what else, if anything, will. Nothing comparable to the telecoms boom of the 1990s is on the horizon, notes Klaus Deutsch of Deutsche Bank Research. Politicians of all stripes tout green technology, but that is speculative, and it is not clear how the government can best nurture it. Hard choices loom in energy among dangerous nuclear power, dirty coal and expensive renewables.

Germany's leaders will handle all this wearing fiscal manacles. Next year's federal deficit is expected to be a record €86 billion ($126.5 billion). The next government, whatever its makeup, will reduce this: members of the euro zone are supposed to limit public-sector deficits to 3% of GDP, and a new constitutional amendment directs the federal government to cut its structural deficit (ie, adjusted for the business cycle) to 0.35% of GDP by 2016. The ageing process makes debt more toxic. The shrinking of the labour force will whittle away at potential growth, consuming the means to pay for it.

A "generation balance" drawn up by Bernd Raffelhüschen and Stefan Moog for the Market Economy Foundation in Berlin weighs the cost of today's spending commitments for tomorrow's taxpayers. The debt of the public sector was 65% of GDP in 2007; adding in unfunded future costs of pensions, health care and other schemes, the state's implicit debt jumps to 250% of GDP. Recent cuts in income tax and social-security contributions softened the crisis but greatly increased the long-term burden. To cope, Germany will have to make the most of its dwindling workforce.

Wasting human capital

By 2020 Germany will lack 2.4m workers, which will cost the economy more than €1 trillion, reckons McKinsey, a consultancy. This sounds a pleasanter problem to deal with than unemployment, more often the spur to reform. There are no real culprits (you cannot denounce childless couples) and the solutions sound cheery: encouraging breeding, improving schools, promoting research and the like. But generational challenges demand reforms almost as daunting as Agenda 2010.

Germany wastes human capital like unmetered water. Despite the reforms, 53% of unemployed people have been jobless for more than a year, more than double the OECD average. A high proportion of women work, but a German obstacle course keeps them from working too much: school hours are short, kindergarten places are scarce and second incomes in families are taxed at high rates. As a result the total number of hours worked in Germany is among the lowest in the OECD.

Around a quarter of children are born into immigrant families, providing a lift to Germany's depressed fertility rate, but they underperform. Children with "migrant backgrounds" drop out of school at more than double the rate of native Germans. Germany's ranking in international tests of reading and maths would jump several places if the scores of migrant children were not counted. Too few Germans of any sort reach the top of the education ladder: 23% of young Germans get university degrees, compared with an OECD average of 36%.

These are the laments of a society that has changed faster than the institutions that are supposed to serve it. The school system is a holdover from an era that deemed motherhood a full-time job, an attitude that France, for example, shed long ago. Only now are Germans getting used to the idea that "guest workers" from Turkey and elsewhere, who arrived from the 1950s onwards, are going to stay. Traditional attitudes have found a home in Ms Merkel's CDU. Although it proclaims that Germany is an "integration land", the party's election programme gives priority to "qualification over immigration", rules out dual citizenship and calls for deporting foreign criminals. On such matters, the SPD is more progressive.

And so, one suspects, is Ms Merkel, for whom being a woman and a one-time physicist seems to matter more than party dogma. Her star appointment was Ursula von der Leyen, a mother of seven, who as family minister introduced "parents' pay", a benefit to encourage middle-class women to bear more children without abandoning their careers. In concert with the states she started a scheme to build pre-schools for all children of parents who want them by 2013, which will help women into the workforce. Ms Merkel brought the government's "integration co-ordinator" into the chancellery and put together an "integration plan" to impart Germany's language and values to immigrants and upgrade their skills.

If Germany is going to defuse the "time bomb" of immigrant dropouts and head off a ruinous skills shortage, it will have to overhaul education. Ms Merkel knows it. But the two main parties are at odds over how to tackle it. The CDU champions the traditional three-tier high-school system, in which pupils are separated early (usually at ten) according to ability. The SPD wants children to study longer together, reckoning that slower ones will benefit. Everyone accepts the goal of raising investment in education from 4.8% of GDP to 7%, but there is no convincing plan to pay for it. The SPD wants schooling to be free, from kindergarten to university; the CDU is more open to charging fees.

Reuters



Overpampered as well as overhatted

Disagreement does not cause deadlock because the *Länder* are free to experiment. Hamburg, for example, which is governed by an unusual coalition between the CDU and the Greens, plans to extend the number of years children study together in mixed-ability primary schools from four years to six. But experiment is risky, as *Länder* governments are discovering. Saarland's CDU government introduced university tuition fees and shut 100 primary schools because there are fewer children to fill them, but that was a big part of the reason the government lost its absolute majority in state elections on August 30th.

Boosting brainpower is not enough. Reform in its narrow sense, of saving on welfare, is unavoidable. The costs of the social-security system are set to soar, in the short term because of the slump and in the long run because the country is ageing so fast. The unemployment-insurance contribution, laboriously scaled back from 6.5% of gross pay to 2.8%, may soon rise, followed perhaps by the health contribution, now 14.9%. That will jeopardise the government's goal of holding total contributions to 40% to encourage employment.

The grand coalition and its SPD-Green predecessor installed checks on the future rise of pension costs (and, in moments of timidity, weakened them). Germany's greying argues for encouraging individuals to rely less on state-funded pensions and more on their own savings, as the FDP advocates. But the real mess is health care. The "generation balance" puts the implicit debt of the health system at 99% of GDP, but that does not include the cost of improvements in medical technology. If you include just half that cost the debt more than doubles, says Mr Raffelhüschen.

The grand coalition dealt with this half-heartedly. Payroll contributions and taxes now flow into a single fund, which distributes the money to insurers according to the number and needs of the patients they enrol. Insurers are supposed to compete for patients; those with high costs may charge a modest additional fee. But real competition has yet to start and may never really happen, since services are uniform and the extra fees are nominal. "The root of the problem still has to be dealt with," says Michael Braun of Mercer, a consultancy. Strife between the CDU and the SPD has prevented a more-coherent solution. A black-yellow coalition might do better.

Too broad a church

A government of determined reformers would not stop there. *Kündigungsschutz*, a system of worker protection that makes each dismissal a judicial adventure, should be loosened, though it is hard to see the cautious Ms Merkel agreeing. One way to reduce the economy's reliance on exports might be to liberalise the *Meisterzwang*, a system of guild protection that restricts competition in some 41 crafts, an idea that the small-business-friendly FDP may resist. The welfare system imposes a steep implicit tax on low-skilled workers, discouraging them from taking jobs. Germany's federal system, which gives states little scope to raise their own revenues and mandates massive transfers among them to even out living standards, is crying out for further reform.

Merely to mention such ideas is to despair of them. Germany has an astonishing capacity to rise to big occasions, such as unification; but in ordinary times it seeks consensus among myriad power centres, which makes progress slow, if it happens at all. A black-yellow government would resist rolling back reform and block some bad ideas, like a generous economy-wide minimum wage. But it would not change the rules.

“I worry about a potential total blockade of the decision-making system,” says Hans-Olaf Henkel, a leader of Konvent für Deutschland, a reformist group. Fewer decisions are now subject to veto by the Bundesrat, the legislative chamber that represents the states. But with more states being governed by coalitions, the Bundesrat’s deliberations could become more tortuous.

The roots of consensus are deep. In the 16th century Catholics and Protestants sought ways to co-operate rather than warring. One ingenious device was the *Simultankirche*, a shared church where the two faiths worshipped separately. Germany itself feels like a secular *Simultankirche*, in which the relative strengths of the sects may change without disturbing the basic arrangements among them. Unfortunately, it will be surprising if this month’s elections break that pattern.

The tyre wars

Playing with fire

Sep 17th 2009 | WASHINGTON, DC AND BEIJING
From The Economist print edition

By succumbing to domestic pressures, America has started an alarming trade row with China

Illustration by KAL



IN RAW economic terms Barack Obama's imposition of tariffs on Chinese tyres hardly registers. The number of jobs affected is barely a rounding error in measurements of the mighty American workforce. The cost to consumers is also slight. But in geopolitical terms, it is a whopper. Mr Obama's most overtly protectionist decision so far has triggered a predictably angry reaction from China, which threatened to retaliate against American chickens and car parts and to haul America before the World Trade Organisation. The *Global Times*, a newspaper that often reflects the views of hardline nationalists in China, ran a front-page headline saying "America has erred before the world".

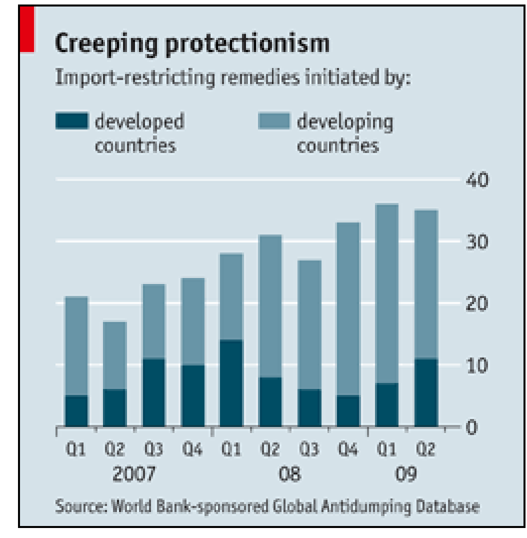
The tit-for-tat dispute casts a pall over the G20 meeting in Pittsburgh on September 24th and 25th where Mr Obama will play host to Hu Jintao, China's president. Warnings of a trade war have multiplied. There have even been comparisons to America's infamous Smoot-Hawley Tariff Act, which deepened the Depression.

Some of this is hyperbole. Smoot-Hawley sharply raised tariffs on thousands of products, not just one. Then, there was no regulating framework for global trade; now both America and China are acting within the WTO, which was created precisely to keep such spats within rules. Every president since Jimmy Carter has sought import restrictions at one time or another, and Mr Obama's are mild by comparison. "On the broad canvas of presidential trade policy, Obama's decision is unexceptional," says Doug Irwin, a trade historian at Dartmouth College. And China's retaliation so far has been measured.

But the decision does come at a risky time. Protectionist actions, in particular against China, have been multiplying in recent years (see chart), even within the confines of WTO rules. Last November George Bush and in April Mr Obama, on both occasions joined by other leaders of the G20, pledged to "refrain from raising new barriers to investment or to trade in goods and services"; yet new barriers have steadily increased.

Until now Mr Obama has tried to allay fears that he is a bit of a

protectionist by abandoning campaign threats to renegotiate the North American Free-Trade Agreement and to punish China for holding down its currency. He has surrounded himself with mainstream, pro-free-trade economists, watered down (though failed to veto) "Buy America" provisions in the fiscal stimulus, and opposed carbon tariffs in the cap-and-trade bill now before Congress. Even now Mr Obama insists he is "committed to pursuing expanded trade and new trade agreements", and this week he defended his action as nothing more than the enforcement of trade laws.



That, however, is a stretch. Mr Obama had no obligation to act. Under the terms of joining the WTO, China gave other countries the right until 2013 to impose temporary "safeguards" against surges of Chinese imports. In America the relevant law, Section 421 of the Trade Act, does not require proof that China has broken international trade rules against subsidising or dumping goods (ie, selling below cost), only that the domestic industry was disrupted. Once the International Trade Commission, an independent panel, says that such disruption has occurred, it is up to the president to decide whether to impose remedies. Mr Bush declined to do so in the four Section 421 cases that came to him.

Politically, Mr Obama may have felt he had little choice. The United Steelworkers union filed the complaint in April and the law required Mr Obama to decide by September 17th. Having promised repeatedly to enforce trade laws more vigorously than Mr Bush, Mr Obama presumably felt he needed to do something. The economic benefits to those who lobbied for protection, however, are minuscule. Domestic manufacturers have largely abandoned the low-end tyre market. The tariffs, which drop from 35% in the first year to 25% in the third, will mostly divert supply to Mexico, India, Indonesia and Brazil, says Tom Prusa, a Rutgers economist who has done work for tyre companies.

China also bears some blame. American negotiators were ready to withhold the tariffs if China made concessions, but to no avail. Mr Obama's defenders note that China would not have gained entry to the WTO without the "safeguard" provisions, which bought political support among its trading partners. And voters and Congress might be less likely to support future trade agreements if the safeguards in existing agreements are never used.

Still, Mr Obama's imposition of tariffs will tempt more industries and unions to seek similar relief, and he will have to decide whether this decision is a template or an exception. Other countries, fearing a wave of diverted Chinese imports, could copy America's action. After Mr Bush raised steel tariffs in 2002, half a dozen other countries followed. Under the terms on which China entered the WTO, others can impose safeguards simply because America has. The European Union, however, would struggle to master enough support among its member states.

China itself faces a delicate balancing act. On September 15th more than 300 of the Communist Party's top officials began a four-day annual meeting in Beijing where, among other things, they are expected to decide whether to give President Hu's presumed successor, Vice-President Xi Jinping, a further boost by making him a deputy commander-in-chief of the armed forces. Succession politics could be complicated by high-level disputes over how to respond to the Americans. And Mr Hu will not want a breakdown of commercial ties with America ahead of the G20 and Mr Obama's visit to China in November.

But nor can he let Mr Obama entirely off the hook. Having announced an investigation into America's alleged dumping, it will be hard to back away. Indeed, the spat will awaken unpleasant memories of the controversy over China's accession to the WTO. China agreed to the safeguards clause in 2001 with gritted teeth, in part because its reformists saw WTO entry as a useful tool for encouraging market-oriented reforms. China's prime minister at the time, Zhu Rongji, was subjected to harsh criticism from conservatives at home for pressing so hard for WTO entry. Times are more difficult now than they were back then, so expect a few more fireworks.

Barack Obama at the United Nations

Saying all the right things

Sep 17th 2009 | WASHINGTON, DC
From The Economist print edition

A love-fest on the East river, harder going in the real world


AP

Hi there, fans

BARACK OBAMA faces squalls at home, but his reputation in most of the rest of the world continues to shine. Next week the president will have a chance to wear these golden opinions in their newest gloss at a parade of meetings at the United Nations in New York. He will chair a summit on climate change, thank countries that have contributed to UN peacekeeping missions, meet African leaders and in general reinforce the message that America is at last under the management of an enthusiastic multilateralist (putting trade to one side, perhaps). On September 24th he will also chair a meeting of the Security Council devoted to nuclear proliferation and disarmament—only the fifth time the council has met at head-of-government level and the first time an American president has chaired it.

Mr Obama excels at public diplomacy. His speech in Cairo in June received rave reviews in much of the Muslim world. But there is more to diplomacy than speeches. The meeting on proliferation cannot but focus attention on the fact that, for all his popularity, Mr Obama has had no more success than the reviled George Bush in persuading North Korea to give up its nuclear weapons or Iran to stop enriching uranium. His promise was to do everything in his power to stop Iran acquiring nuclear weapons, while also extending his hand to countries that unclenched their fists. But his policy of engagement has so far yielded no result.

Two letters from Mr Obama to Ayatollah Ali Khamenei, Iran's supreme leader, are reported to have received a dusty answer. The rigging of Iran's elections in June and the violent repression that followed have made further overtures harder. Indeed, some Iran-watchers in America accuse Mr Obama of inadvertently speeding up this sequence of events by opening a dialogue that has emboldened Tehran's hardliners. He is soldiering on nonetheless. America has just announced that it will take part next month in direct talks with Iran (albeit with Britain, France, Germany, China and Russia at the table, too).

This, said a State Department official, was being done "without illusions…our patience isn't infinite." But it is not clear what Mr Obama will do if, as seems likely, Iran continues to defy the Security Council's orders to stop enriching uranium, and when America's patience does at last run out. Despite bold talk in Washington about imposing "crippling" economic sanctions, Russia and China have given no sign of helping Mr Obama any more in this regard than they did the less popular Mr Bush.

George Mitchell, America's Middle East envoy, has meanwhile been shuttling around the region in the hope of extracting a settlement freeze from Israel's prime minister, Binyamin Netanyahu, in exchange for the Arab states taking steps toward "normalising" relations with the Jewish state. The administration hopes that if Mr Mitchell can close this deal in time, Mr Obama will be able in New York next week to inaugurate peace talks between Mr Netanyahu and the Palestinians' president, Mahmoud Abbas. But even then Mr Obama would be a long way from a breakthrough. Amid much fanfare, Mr Bush launched peace talks between Israel and Mr Abbas at Annapolis at the end of 2007. The two sides talked and talked—and got nowhere.

For many of his admirers around the world, the truest test of Mr Obama will not be whether he can make a breakthrough in the incorrigible Middle East, but whether a president who acknowledges the overwhelming danger of global warming can galvanise multilateral action on climate change. There too, however, public diplomacy has its limits. Mr Obama's eloquence may blow away his audience in New York. But foreign governments know that, with less than three months to go before the world's climate summit in Copenhagen, the Democrats' cap-and-trade bill faces an uphill battle in Congress. A president who cannot reduce America's own carbon emissions will not easily persuade other countries to do so, no matter how much people like him.



Health-care reform

Half a loaf—or just half-baked?

Sep 17th 2009 | NEW YORK
From The Economist print edition

A long-awaited plan



Reuters

WHEN Barack Obama outlined his vision for health reform to Congress on September 9th, he insisted that any bill must cut the uninsured by 30m, cost only $900 billion and raise the federal deficit not "one dime". The leading congressional bills thus far fail the test, but Max Baucus, the head of the Senate's powerful Finance Committee, now says he can pull this off.

After intense bipartisan negotiations, Mr Baucus (pictured) unveiled his bill on September 16th. His effort would force most Americans to obtain cover, but in return insurers must agree not to drop coverage because customers have "pre-existing conditions" or because spending caps have been reached.

To expand coverage, the plan would create internet-based marketplaces that would simplify and standardise insurance offerings. It would also offer refundable tax credits to families earning up to 400% of the federal poverty level, on a sliding scale, to help them buy insurance. Mr Baucus would also expand Medicaid, an existing health-insurance scheme for the poorest Americans, to cover more of them.

On cost, the bill appears at first blush to offer a breakthrough. The Congressional Budget Office (CBO), a non-partisan agency, claimed this week that his plan will actually reduce the federal deficit by $16 billion in 2019, and slash deficits over the subsequent decade by half a percent of GDP versus the current trend. Previous proposed health-reform bills have failed this test, with the version now pending in the House being far too expensive for Mr Obama to sign in its current form.

The agency estimates that the plan would expand coverage to some 29m currently uninsured people over the next decade, at a total gross cost of only $774 billion. And thanks to all the revenue earned by a new tax on pricey insurance plans, fees to be levied on medical industries and big cost savings to come from cuts in Medicare (the government health scheme for the elderly), these costs are supposedly more than offset.

Alas, this is too good to be true. A flaw is that the Baucus plan, like its chief rivals, does too little to fix the perverse incentives driving up health costs in the first place. Two more immediate snags may also trip it up: fuzzy maths and petty partisanship.

One problem is that some claimed savings are unrealistic. The plan assumes, for example, that payments made by Medicare to doctors will be cut by nearly 25% in 2011. Senator Judd Gregg scoffs that the "claim of deficit-neutrality is dependent on Congress's willingness to follow through on painful cuts they have been unwilling to follow through on in the past." And the medical-devices industry is already gearing up to escape some of the $40 billion in taxes to be slapped on it.

The other obstacle is partisan bickering. Laudably, Mr Baucus has pursued a moderate course, rejecting a proposal for a government-run insurance scheme. But this and other concessions (on malpractice reform, for example) have failed to win him a single Republican endorsement thus far. Worse yet, such concessions have attracted the ire of such liberals as Senator John Rockefeller, who declared this week that the Baucus bill "will not have my vote".

Still, it is too early to count the bill out. The full Finance Committee will consider it next week. Stephanie Herseth Sandlin, a leader of the Blue Dog coalition of conservative Democrats in the House, thinks it is "an

important step forward." And Olympia Snowe, a Republican moderate member of the committee whose vote could make all the difference, says it "moves in the right direction." Faint praise; but an imperfect bill's saving grace may be the fact that it is better than the alternatives.

Political memoirs

In their own words

Sep 17th 2009 | CHICAGO
From The Economist print edition

Politicians try to rewrite history

THE truth will set you free—so says Jesus in the Gospel of St John, and so says Rod Blagojevich in "The Governor". The ousted chief executive of Illinois has written a new book, a political memoir that invaded America's bookshops on September 8th. It will soon have plenty of company. Virtually every member of George Bush's White House is writing a book. Condoleezza Rice has a deal to write three. And the late Edward Kennedy's tome is already occupying the shop windows (see article).

Politicians are fond of writing memoirs for many reasons. First, books by the famous make money. Bill Clinton earned a $15m advance for "My Life", published in 2004. But a politician also writes to solidify his legacy or, in some cases, reshape it. Critical books abound about the Bush presidency, from Bob Woodward's tomes to "Duck! The Dick Cheney Survival Bible". Now Mr Bush is telling his side of the story: the self-described "Decider" is writing about his most important decisions. Dick Cheney, the former vice-president, who is said to be scrawling his memoir on yellow legal pads, explains that a book will help his grandchildren understand his actions.

There is scant evidence, however, that autobiographies change the public's views. Memoirs by presidents, in particular, are likely to be bland. The first sections of Mr Clinton's book are interesting enough, but the main conclusion from "My Life" is that it makes an excellent doorstop. "Dreams From My Father" is fascinating precisely because Barack Obama wrote it long before becoming president. Perhaps the last illuminating memoir by a former president was written 124 years ago, by Ulysses Grant.

Mr Blagojevich sets a new standard in the genre, as in most areas to which he applies himself. In December 2008 Chicago's busiest publishing house, that of the federal prosecutors, released a complaint that accused Mr Blagojevich of trying to sell Mr Obama's Senate seat. Mr Blagojevich offers a rebuttal in "The Governor" that involves quoting Harry Truman, Aeschylus, and Rodgers and Hammerstein, while he likens himself to Columbus, Jimmy Stewart, Henry V and Icarus to Mr Obama's Zeus.

Writing the book was not a sound legal move; prosecutors can use quotations during cross-examination. But "The Governor" won Mr Blagojevich a six-figure advance and a series of interviews. "The general thing to remember," says Dick Simpson of the University of Illinois at Chicago, "is that politicians want to be loved. That's why they were in politics in the first place."

Gloomy numbers from the census

Poorer, but at least not sicker

Sep 17th 2009 | WASHINGTON, DC
From The Economist print edition

Measuring the recession's bitemarks

READING a census report is like peering through a telescope from the back of a speeding train. You can see what's behind you but not where you are, let alone what's ahead. The latest numbers on income, poverty and health in the United States, released on September 10th, are pretty gloomy. But most economists think things have got even worse since they were gathered.

Between 2007 and 2008 real median household income in the United States fell by 3.6%, from $52,163 to $50,303. Worst-hit were Hispanic households, whose incomes fell by 5.6% to $37,913. Asian-Americans, as usual, were comfortably at the top of the heap with a median household income of $65,637, though this had fallen by 4.4% in a year. The figure for non-Hispanic whites fell by 2.6% to $55,530, while for blacks it declined 2.8% to $34,218.

The proportion of people without health insurance remained unchanged, at 15.4%. Although private-sector workers lost coverage, the number of people covered by the government rose from 83m to 87m. The share of children without insurance, at 9.9%, was the lowest since 1987.

The official poverty rate rose slightly, from 12.5% to 13.2%, bringing the total to 39.8m people. This was the first statistically significant annual increase since 2004. But the official poverty measure ignores many government benefits. For example, if the cash value of food stamps were accounted for, there would have been 1.7m fewer poor people in 2007. If the earned-income tax credit (a cash transfer to the working poor) were included, 2.4m children would have been lifted out of poverty. The official poverty measure is politically untouchable because it is used to allocate heaps of public money. However, the Census Bureau, aware of its shortcomings, has added a calculator to its website to let people work out their own measures.

Ben Bernanke, the chairman of the Federal Reserve, said this week that the recession was probably over. But unemployment could stay high even as output recovers, reckons Isabel Sawhill of the Brookings Institution, a think-tank. She thinks the poverty rate will peak above 14% and stay as high as 13% for a decade or so. Joblessness can scar those who experience it, she worries. People's skills deteriorate and they may eventually become discouraged from seeking work.

Doug Besharov of the University of Maryland thinks the big (and politically important) problem is not so much the addition of a couple of million people to the poverty rolls but the "giant hit" the recession has inflicted on the middle class. They have lost a fortune, as the value of their homes and retirement portfolios has tumbled. And some 8m Americans have lost their jobs since late 2007. Assuming that most have families, perhaps 30m people have been intimately affected by the great downsizing. A big surge in joblessness does not necessarily show up in the poverty statistics, because many of those downsized are men with working wives. But 30m people is a lot of voters, says Mr Besharov. "These people don't think of themselves as poor, but they are hurting, they feel wronged and they want government help," he says.

Illegal immigration

The continuing crackdown

Sep 17th 2009 | AUSTIN
From The Economist print edition

Some local authorities are keen to help rumble illegal immigrants

Getty Images



Calling for help

FULL-SCALE immigration reform is clearly on the back-burner. But the Obama administration has been tinkering with immigration policy all year, and now it has announced another tweak. The Department of Homeland Security (DHS) wants more people to use section 287(g) of the Immigration and Nationality Act. The programme, commonly known as 287(g), says that state and local authorities can have some of their officers trained to enforce immigration laws. Over the past several years 66 state and local agencies have signed up, from the Missouri Highway Patrol to the police department of Framingham, Massachusetts. Nobody likes criminal aliens and Janet Napolitano, the secretary of homeland security, reckons that 287(g) is an effective "force multiplier." But expanding the use of 287(g) is turning out to be rather unpopular.

The idea is that police and sheriffs can help the feds capture the bad guys. In practice 287(g) has suffered from mission creep. A report in January from the Government Accountability Office found that the programme lacked internal controls, with the result that the extra 287(g) officers were gumming up the works by catching minor traffic-offenders rather than genuinely criminal aliens. Many activists had hoped that Mr Obama would end the programme. Instead, his administration has embraced it.

The announcement has also outraged immigrant-rights advocates and civil-liberties groups. They maintain that 287(g) is arbitrary and punitive. Marielena Hincapié, the executive director of the National Immigration Law Centre, argues that it actually makes communities less safe because it weakens an already strained relationship between undocumented people and law-enforcers. Crime victims and witnesses are likely to be reluctant to come forward if they fear that they may be deported for their pains.

Section 287(g) is also vulnerable to abuse. One of the programme's biggest fans is Joe Arpaio, the notoriously tough sheriff of Maricopa County in Arizona. He is under investigation by the Justice Department on allegations that his version of law-enforcement involves racial profiling—picking on Hispanics, in short. Anything that mixes up illegal-immigrant control with ordinary policing clearly runs that risk. Expanding enforcement—or so the president's critics say—is a poor substitute for full-scale reform.

The revival of Pittsburgh

Lessons for the G20

Sep 17th 2009 | PITTSBURGH
From The Economist print edition

The city of bridges has built a bridge from its steel past to a diverse 21st century economy. The summiteers arriving on September 24th can take note

UPMC



EVEN on an overcast day, the view from Jeffrey Romoff's office is spectacular. Across the river are waterfront baseball and football stadiums. Dozens of bridges span the Allegheny to the north-east and Monongahela to the south-east. The two rivers merge to form the Ohio River. Not one soot-churning mill is in sight. Ed Rendell, Pennsylvania's governor, observed that it used to be "you couldn't see a bloody thing". Steel was once the largest employer in the region. Now the University of Pittsburgh Medical Centre (UPMC), an $8 billion health-care conglomerate, is western Pennsylvania's biggest employer, with 50,000 people. Last year Mr Romoff, UPMC's chief executive, moved his headquarters to the old US Steel tower, the city's tallest building. UPMC's logo now sits on top of it.

Pittsburgh does not rely solely on UPMC or the health industry the way it once leant on steel. When the steel industry collapsed in the early 1980s, the city and region lost 120,000, or about half, of all its manufacturing jobs. Some 50,000 Pittsburghers left the region annually. The city's revival since then has been part organic and part good long-term planning. State and local officials provided investment, while universities and community and corporate leaders came together to develop economic and business strategies for the region. Pittsburgh's employment has, over the ensuing three decades, diversified quite well.

Leaders from the world's 19 largest economies plus the European Union will be in Pittsburgh on September 24th and 25th. When the White House press corps heard the G20 was to be hosted by Pittsburgh, many sniggered. Usually such meetings are held in capitals like Beijing or London, not rustbelt cities. But, as Barack Obama said on September 8th, Pittsburgh has "transformed itself from the city of steel to a centre for high-tech innovation—including green technology, education and training, and research and development."

Today, its main industries, health care and education, are thriving. Pittsburgh's health-services business has almost tripled in size since 1979, creating more than 100,000 jobs. More than 70,000 work in research and development in the metro area's 35 universities (Jonas Salk produced the polio vaccine at the University of Pittsburgh in 1955) and 100 corporate research centres, such as that of Bayer usa, a pharmaceuticals company. Greg Babe, its head, says six jobs rely on one Bayer job.

Pittsburgh has changed itself physically too. The waterfront, once lined with factories, has been given over to parks. The building hosting the G20 is the world's first and largest LEED-certified (meaning green) convention centre and sits on the city's former red-light district. Pittsburgh Life Sciences Greenhouse, which provides investment and advice to the region's bioscience firms, is housed on a redeveloped brownfield, the former site of a strip-mill. SouthSide Works is a 123-acre (50-hectare) development made up of shops, offices, hotels and apartments that sits on the former site of an LTV Steel plant. Manufacturing continues to employ 8% of the workforce and the city is still home to US Steel. It is also a centre for innovation in robotics, electronics and nanotechnology.

Entrepreneurship has been fostered. Innovation Works, a state-aided seed fund, supports firms in their earliest stages of development. Susan Catalano, a neurobiologist working to stop Alzheimer's symptoms, moved her start-up to Pittsburgh's South Side to take advantage of this help. Thanks to universities of the stature of Carnegie Mellon and the University of Pittsburgh, many new companies and recruits are drawn in. Pittsburgh's unemployment rate, at 7.8% in July, was lower than the national rate of 9.4%.

Forbes magazine recently named Pittsburgh as one of America's best cities for job growth. Some 30,000 jobs are available in the region, says Bill Flanagan, of the Allegheny Conference, an economic development group, an increase of 10,000 since the beginning of 2009. Pittsburgh has 8.4% of the

nation's nuclear engineers. Westinghouse, a nuclear-power company, is on a hiring spree. People are drawn to the region's well-paid jobs, low cost of living and good schools. The EIU, a sister company of *The Economist*, ranked it the most liveable city in America. It boasts the top-flight Pittsburgh Symphony Orchestra and the Pittsburgh Opera, as well as a host of theatres. Gorgeous Victorian townhouses can be bought for amazing prices.

Thanks to a thriving economy and a minor budget surplus, Pittsburgh looks set to stay in good shape. It largely missed the housing and dotcom booms and busts endured by the rest of the country. In fact, it is currently building a new sports arena, a new hospital and, for the first time in decades, housing in the downtown area. Because of a 2003 brush with bankruptcy, it cut its municipal workforce by a quarter, and took many hard decisions, such as closing fire stations, making it well-placed to cope with the current recession.

As well as 1,100 delegates and 2,000 journalists, the city is preparing itself for an onslaught of protesters. One website, resistg20.org, promises a mass march and other protests to disrupt the summit. Some 35,000 people rallied at the G20's April meeting in London. Luke Ravenstahl, the city's 29-year-old mayor, is quadrupling the 900-strong police force by shipping in 1,500 state troopers and borrowing cops from cities like New York. The city's businessmen and politicians are hoping that the protesters and the politicians won't wholly eclipse their own impressive tale of transformation.

Lexington

Charlie Rangel's taxes

Sep 17th 2009
From The Economist print edition

Those who write laws should obey them

Illustration by KAL



IT WAS so cold that rifles jammed and blood froze in men's wounds. Chinese soldiers were cascading across the border into Korea. The Americans in their path were helplessly outnumbered. Private Charlie Rangel was lying in a gully where an explosion had tossed him, punctured with shrapnel and scared to death. He told Jesus that if he ever got out of this mess, he would "never be a problem to anybody, ever again." He thought he heard Jesus reply: "Boy, if you want any help you'd better get out of that hole."

So he crawled over a ridge, where he found his comrades panicking. "What should we do, Sarge?" they hollered. Private Rangel was not a sergeant, but he had an air about him, a mixture of bravado and charisma, that made people think he was. And since these terrified 18-year-olds expected him to lead them, he did: over a mountain, through enemy lines and to safety. "Because I appeared to be less scared than the 43 enlisted men who followed me, I received the Bronze Star," he recalls.

Mr Rangel is a war hero. But his ascent from the streets of Harlem to the corridors of Congress is, in some ways, even more impressive. His father was "absolutely no good", he says in his memoirs. At the age of five or six, he tried to stop him from beating his mother by hitting him with a broom. When his father walked out and his mother had to travel to work, young Charlie was sometimes left with uncles who got drunk and lost him. He hung out with hoodlums. But he also hung out with altar boys ("I was running after their fine and proper Catholic schoolgirls," he explains). And when the two groups met, he mediated, sometimes persuading his criminal friends to give his Catholic friends their watches back.

Before the Korean war, he was a high-school dropout. Afterwards, he used the GI bill to put himself through college. He decided to become a lawyer because his grandfather, who worked the lift at a courthouse, admired lawyers. He went into politics because he had a flair for it. (At law school, he says, he orchestrated ethnic factions "like Toscanini conducting Beethoven's Ninth".) He was elected to Congress in 1970. Since 2007, he has been chairman of the mighty House Ways and Means Committee, which writes the nation's tax laws. And alas, he is now accused of failing to obey those laws.

Mr Rangel owns a villa in the Dominican Republic, but forgot to report or pay taxes on $75,000 of rental income from it. He occupies four rent-controlled apartments in New York, courtesy of a developer. When disclosing his assets to Congress, he appears to have omitted roughly half of them, including an account with at least $250,000 in it. The *New York Times*, which is seldom in the vanguard of witch-hunts against

Democrats, has already urged him to resign his chairmanship. So, in blunter language, did many of the tens of thousands of "tea party" protesters who flocked to Washington on September 12th to complain about big government. Some chanted "Boot Rangel!" A typical placard showed Mr Rangel and Tim Geithner, the treasury secretary, who also neglected to pay some of his taxes, with the slogan: "The best tax advisers I've ever had".

For now, Mr Rangel is holding tightly to his chair, insisting that any errors were inadvertent and that no one should prejudge the results of two congressional probes. His admirers are appalled that such an immense figure might fall over a few instances of sloppy book-keeping. This is a man who marched with Martin Luther King. He changed the tax code to make sanctions against apartheid South Africa bite. He created "empowerment zones" to boost inner cities. He fought to expand the "earned-income tax credit", which helps the working poor. And he is still fighting doughtily for health reform. "This has nothing to do with black, white, Republican [or] Democrat," he said this week. "It has to do with the fiscal survival of our nation."

Rage against the machine

Mr Rangel's critics will have none of this. But some comfort themselves with the belief that he is the last of a dying breed of machine politician. He owed his first job in politics to a Tammany Hall boss. He cut deals with Nelson Rockefeller, the Republican governor of New York, who in 1970 handed him a pencil and let him draw his own congressional district. He runs a big patronage network and never has to worry about re-election. But he is nearly 80, and the new generation of politicians are different.

Or are they? Steven Malanga of the Manhattan Institute, a conservative think-tank, argues that they are worse. Old-style political bosses handed out patronage jobs here and there, he says. Their modern counterparts lavish huge sums on groups that support them. And some of these groups are a bit iffy. A reporter posing as a pimp recently filmed staff (since fired) at a radical group called ACORN advising him to claim some of the underage prostitutes working for him as dependants for tax purposes. ACORN, alongside which the young Barack Obama worked on voter-registration in the 1990s, has received tens of millions of taxpayer dollars. It is not only the tea-party protesters who figure that, if this is what the government does with their hard-earned money, they would rather keep it.

Which is why, for all Mr Rangel's charm and back-room savvy, he is now an obstacle to his party's agenda. Mr Obama insists that health-care reform will not add to the deficit, and that only the rich will pay more taxes. But few Americans believe him. Some 91% of Republicans, 71% of independents and even 48% of Democrats expect their tax bills to rise, reckons Gallup. If Democrats want to get anything done this year, they must heed such fears. And if they want everyone to pay a fair share, they need leaders who are seen to do likewise. Mr Rangel should resign.

Economist.com/blogs/lexington

Chile's presidential election

The strange chill in Chile

Sep 17th 2009 | SANTIAGO
From The Economist print edition

After presiding over Latin America's big success story for two decades, the centre-left Concertación coalition looks tired and divided

Alamy



ALONGSIDE an urban motorway in Lo Espejo, a crowded working-class district of Santiago, Chile's capital, builders are labouring in the mud of the southern-hemisphere winter to complete 125 new houses of brick and timber. In the next few weeks families from the dilapidated huts that once stood on the site will move in. The poorest among them will pay just $400 for a house costing about $20,000, part of a government policy aimed at abolishing the last remaining shantytowns in Chile by next year. They are among the 600,000 families who will have received housing grants during the four-year term of Chile's president, Michelle Bachelet, which ends in March.

This year the programme has been expanded, as part of a fiscal stimulus totalling $4 billion (or 2.8% of GDP). This has not prevented recession: in the second quarter the economy was 4.5% smaller than in the same period last year. But it has mitigated its effects. Some 270,000 building workers are now employed on social-housing schemes, up from 145,000 a year ago. "All these projects are helping the unemployed," says Willy Gutiérrez, a carpenter at the site in Lo Espejo.

They have also lifted the popularity of Ms Bachelet, a Socialist (see article). Despite the recession, her approval rating has soared to 72%, up from 40% in June 2008, according to polls by the Centre for Public Studies (CEP), a think-tank. So has that of her finance minister, Andrés Velasco, a liberal former Harvard professor. If the constitution did not prohibit consecutive terms, Ms Bachelet would be strongly placed to win the presidential election in December. As it is, her centre-left coalition, called the Concertación, risks losing power for the first time since democracy was restored in Chile in 1990.

As campaigning formally got under way on September 15th, the latest CEP poll gave Sebastián Piñera, the businessman candidate of the conservative opposition, 37% of the vote. Eduardo Frei, a Christian Democrat who was Chile's president from 1994-2000 and is the official Concertación candidate, trailed on 28%, while Marco Enríquez-Ominami, a dissident Socialist congressman standing as an independent, had 17%. The past four presidential elections mirrored the result of a plebiscite in 1988 in which 56% of voters backed a return to democracy, whereas 44% wanted General Augusto Pinochet's 16-year dictatorship to continue. Will this one break the most stable political pattern in Latin America?

Under the Concertación, Chile has been the region's big success story, adding an increasingly robust

democracy and welfare provision to the free-market economic policies bequeathed by Pinochet. In the 20 years to 2006, the poverty rate fell from 45% of the population to just 13.7%. Income distribution remains highly unequal but opportunities are widening. Eight out of ten youths now finish secondary school. Four out of ten go on to higher education and of these 70% are the first in their families to do so, in many cases thanks to government-backed grants or loans, points out Mr Velasco.

Thanks to its prudent macroeconomic policies, Chile was able to do more than many of its neighbours when recession struck last year. The Concertación has written into law a fiscal rule requiring the government to balance the budget over the economic cycle. It has paid for the large fiscal stimulus by drawing on savings piled up when the price of copper, the main export and a big source of government revenue, reached record levels in the early years of Ms Bachelet's term.

Yet despite all these achievements, the sense of malaise in Chile is as palpable as the snow blanketing the Andes. Businessmen worry that the economy is no longer the most dynamic in South America (see chart). For years politicians have talked of the urgent need to improve the dismal quality of education and invest more in innovation and research and development if Chile is to become a developed country. They are still talking about it.

"We've gone from the Chilean miracle to the Chilean siesta," declares Mr Piñera. He would keep the fiscal rule and the social-protection net, he says. But he accuses the Concertación of, in essence, caging the animal spirits of entrepreneurship. Pointing to falling productivity, he blames rigid labour legislation and the mismanagement of public investment (where $10 billion has been wasted in the past four years, he claims, citing the botched overhaul of the railway network and Santiago's public transport). His economic adviser, Felipe Larraín, says that a Piñera government would raise the annual rate of growth to 6%, boosting productivity through tax breaks for investment, a more flexible labour market and civil-service reforms.



Mr Velasco counters that as Chile gets richer—its income per head was $10,100 in 2008—it is harder for the country to grow as fast. If Chile continues to progress at around 4% a year, that would be broadly in line with the performance of such successful economies as Finland and South Korea at the equivalent stage in their development. He points out that investment and productivity always fall during a recession. Public investment on research and development is rising. Chile continues to score highly in international league tables of competitiveness and the ease of doing business. And growth has been clipped partly by rising energy costs after Argentina ended gas exports to its neighbour.

The Concertación is more vulnerable to the charge that in its way of doing politics it has lost touch with ordinary Chileans. That is the main argument of Mr Enríquez-Ominami. Aged just 36, he describes himself as "an illegitimate child" of the ruling coalition. His father was a guerrilla leader killed by the Pinochet regime. His stepfather is a Socialist senator; his mother's grandfather was a founder of the Christian Democrats. He grew up in France, returning to become a television director. His boyish good looks, charm and speed of phrase make him "one of the best communicators Chilean politics has ever had," writes Patricio Navia, a political scientist, in a forthcoming book.

The young desert politics

Mr Enríquez-Ominami's thinking is a shallow mixture of social liberalism and old-fashioned social democracy. But he, rather than his policies, is the message. His candidacy is a protest against the Concertación's failure to hold a national primary election and against what he sees as the domination of ageing and unaccountable party bosses. He wants a political reform, partly to sweep away the electoral system of two-member constituencies bequeathed by Pinochet. This is widely reckoned to cement the power of the party bosses, block minority parties and prevent political renewal. It has contributed to a worrying alienation from politics among younger Chileans. Almost a third of adults have not bothered to register to vote (this is voluntary in Chile).

Nearly all political commentators in Chile reckon that Mr Enríquez-Ominami cannot win. But he has made Mr Frei, a decent and competent man, look reactionary and old (he is 67). His response has been to promote young advisers and espouse many of his opponents' arguments, such as the need for political

reform, changes to the labour code and modernisation of the state. He is the only one who could actually get these things done, he claims.

All three candidates agree that Chilean society has changed faster than the state and the political system. After 20 years, a change at the top would hardly be surprising. But the right has not won a presidential election in Chile since 1958. Mr Piñera and Mr Frei will almost certainly go through to a run-off election in January—a contest that either man could win.

Chile's surprising president

The Bachelet model

Sep 17th 2009 | SANTIAGO
From The Economist print edition

A politician on top of her game

Reuters



Much more to smile about now

WHEN she was elected as Chile's president in January 2006 Michelle Bachelet promised to be a different kind of politician. A paediatrician and twice-separated mother of three children, she was the first woman to be elected to the top job in a Latin American country who was not the widow of an illustrious husband. She promised a "citizens' democracy" of greater participation. Her first cabinet was selected according to gender as much as party: half its members were women, several were independents and only two had previous ministerial experience.

She quickly ran into troubles, ranging from protests by schoolchildren to transport chaos in Santiago. A year ago, her Concertación coalition lost a municipal election—its first-ever defeat. She is barred from standing in the coming presidential election, yet if the Concertación wins, it will be partly down to Ms Bachelet. She has evolved into one of the most formidable political leaders in Latin America. When *The Economist* went to see her in La Moneda, the presidential palace, she was relaxed and unhurried, keen to answer questions at length rather than in sound bites.

What explains her change of political fortune? Her consultative method of leadership may have looked like "weakness" to traditionalists, partly because "women speak more softly," she concedes. "There is still a lot of *machismo* and sexism." But Chileans have come to see her as empathetic, as a mother figure who is protecting them, and who had been "in command" when recession struck, she adds. In practice, however, she has been forced into some compromises, bringing political heavyweights into the cabinet, and delegating more.

A second reason is that, while sticking to fiscal rigour (at some political cost), she opted to make social protection and the promotion of equality of opportunity her main priority. Her government is building 3,500 crèches for poorer children. It has introduced a universal minimum state pension and extended free health care to cover many serious conditions. Its housing policy features better-quality homes, in model neighbourhoods. But its efforts to shake up education have been disappointingly timid.

It will take time and study before it is clear whether these programmes work. Certainly, it was a while before they made their mark in Chile—"a crèche isn't sexy," says Ms Bachelet. But it adds up to one of the most far-reaching attempts to combine economic growth and a welfare state in Latin America. That is a tacit critique of Hugo Chávez's contention that only his revolution can tackle inequality in the region. And it suggests that Ms Bachelet's political career is far from over.

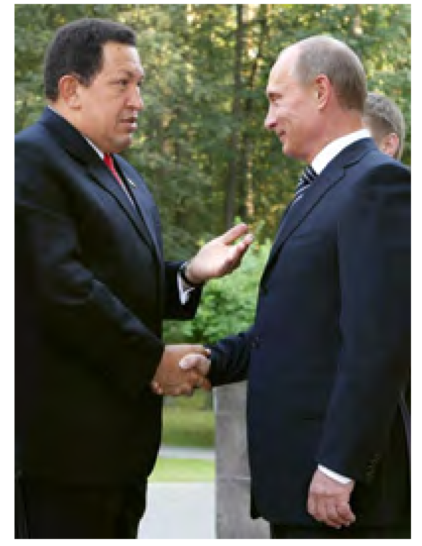
Venezuela's foreign policy

Dreams of a different world

Sep 17th 2009 | CARACAS
From The Economist print edition

Arms and the tyrants

EPA



Putin finds a customer for his missiles

AFTER a two-week tour that included stops in Libya, Algeria, Syria, Iran, Turkmenistan, Belarus and Russia, where he placed orders for tanks and missiles, Hugo Chávez this week got what he seemed to be seeking all along: the attention of the United States. Hillary Clinton, the secretary of state, worried that Venezuela's weapons' purchases might trigger an "arms race" in Latin America, and her spokesman described Mr Chávez's actions as a "serious challenge to stability".

Nowadays Mr Chávez's foreign policy gives top priority—outside Latin America—to forging an anti-American political alliance with Iran, Syria, Belarus and Russia. Mr Chávez told *Le Figaro*, a French newspaper, that he had clinched a deal on nuclear co-operation with his Iranian counterpart, Mahmoud Ahmadinejad. In response, France's foreign minister reminded Venezuela that a United Nations resolution forbids Iran exporting material from its controversial nuclear programme, of which Mr Chávez is a supporter.

Robert Morgenthau, Manhattan's veteran district attorney, told an audience in Washington, DC, earlier this month that Venezuela's alliance with Iran was a direct threat to American interests. Bank accounts in Andorra, supposedly belonging to people close to Mr Chávez, have been frozen at the request of the United States Treasury, reportedly because of suspicions of links to terrorism.

But the more immediately worrying development may be Venezuela's arms build-up. Mr Chávez has already spent at least $4.4 billion on Russian fighter jets, military helicopters and rifles. This month he said he had ordered 92 tanks and anti-aircraft missiles using a $2.2 billion loan from Russia. Press reports say three submarines may follow.

The Venezuelan army's tanks are in poor shape: the president was said to be shocked last year when he ordered them to the Colombian border only to find that few completed the journey, according to a foreign diplomat. The missiles seem to be a hasty response to an agreement last month under which Colombia gave the United States facilities at seven bases for anti-drug operations. Mr Chávez chose to see this as a threat. The missile batteries would make it "very difficult for foreign aircraft to come and bomb us", he said. But his own buys will in turn alarm Colombia.

In Moscow Mr Chávez played up his claim that Russia and Venezuela were "strategic allies", and followed the Kremlin in recognising the independence of the enclaves of Abkhazia and South Ossetia, carved from Georgia last year by Russian troops. But Russia's leaders seem to see Mr Chávez primarily as a useful customer for their arms industry.

Mr Chávez offers his allies oil and gas. He promised Iran 20,000 barrels a day of petrol, even though Venezuela's refineries are struggling to supply the local market. He granted Russia's national energy consortium a block in the Orinoco heavy-oil belt. On the way home he dropped in on Spain's leaders just as Repsol, a Spanish company, announced the discovery of a big natural-gas field in Venezuelan waters.

Closer to home, Mr Chávez's plans have come unstuck. His application to join the Mercosur trade block has stalled in Brazil's Senate. His anti-American alliance, called ALBA, lost a member with the coup in Honduras in June. This week he once again failed to obtain an explicit condemnation of Colombia's base agreement with the United States from Unasur, the Union of South American Nations.

Government policy documents suggest that Mr Chávez's aim is to stir up troubles for the United States in

many places at once, eventually bringing about the collapse of what he calls "the empire". Most of the regimes he is cultivating in this enterprise are marked by rigged elections, media censorship, the criminalisation of dissent and leaders for life. Is that the future of Venezuela?

Homophobia in Jamaica

A vicious intolerance

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From The Economist print edition

The politicians seem unperturbed by hate crimes

IT MAY have a laid-back image of reggae and Rastas, sun and sand. But for gays, Jamaica is closer to hell. The latest apparent victim of homophobia on the island was Britain's honorary consul in Montego Bay, the tourist centre, strangled in bed at home on September 9th. A note denounced him as homosexual.

Openly gay people must contend with the constant fear of violence. The Jamaica Forum for Lesbians, All-Sexuals and Gays (J-FLAG), a pressure group, reports 33 cases of serious injuries from mob attacks on gays in 18 months. Two female couples were attacked and raped by men in recent weeks. Many attacks go unreported, partly because police do not always investigate them. In court a murder charge is likely to be reduced to manslaughter if the victim was gay and the defendant claims provocation, as happened with the killer of an Anglican priest stabbed in his vicarage in 2006.

Some Jamaican gays say the police are becoming more helpful. Lyrics threatening death to gays by popular dance-hall artists have become much less common since the Broadcasting Commission of Jamaica, a regulator, decided in February to block all "lewd" and violent content. These lyrics also attracted bans and fines abroad.

But this does not herald a serious outbreak of tolerance. What Jamaican law calls "the abominable crime of buggery" is punishable with up to ten years of hard labour; "gross indecency" merits up to two years. A reform of sex legislation is now before parliament. But under pressure from the churches, both government and opposition have taken pains to weed out any wording that might weaken the ban on gay sex.

The prime minister, Bruce Golding, told parliament that he would not yield to foreign pressure to liberalise the law. One of his backbenchers Ernest Smith called for J-FLAG to be outlawed, and gave warning that gays were infiltrating the police.

The violence is feeding a gay "brain drain", with some of the brightest Jamaicans leaving for the United States or Canada. Even if they do not care about human rights, Jamaica's politicians and its government might spare a thought for the impact of their intolerance on a chronically stagnant economy.

Thailand's political army

Where power lies

Sep 17th 2009 | BANGKOK
From The Economist print edition

Coups are such an old-fashioned way of running things

Getty Images



AUTUMN in Thailand is coup season. Three years ago the prime minister at the time, Thaksin Shinawatra, flew to New York for the United Nations General Assembly as rumours circulated in Bangkok of a plot against him. His army chief denied them. On September 19th 2006 he seized power. As he sets off for this year's UN meetings, the current prime minister, Abhisit Vejjajiva, will be hoping that history does not repeat itself. Since Mr Thaksin's ousting, Thailand has been convulsed by political fighting. The army has played a decisive role, even after it donned a figleaf of civilian rule. Few expect the generals to go back to their barracks soon.

To mark the third anniversary of the coup, Mr Thaksin's red-shirted supporters plan to rally in Bangkok. A big show of force is likely. A controversial security law allows troops to restore order if the police cannot manage—and a political row over the appointment of a new police chief has already rattled the force.

Mr Abhisit has tried to reassure nervous Thais that his squabbling, nine-month-old coalition government is on good terms with the army. The top brass have given their usual no-coup pledges. This time, they are probably sincere. It would seem rash to unseat Mr Abhisit, whom they helped to install after the courts dissolved a pro-Thaksin government, and who remains beholden to them.

Army officers like to grumble that politics in Thailand, unlike soldiering, is a dirty game. But it is a game that they have rigged to their advantage. After the coup, the liberal 1997 constitution was replaced by a less democratic one. They have secured a bigger budget allocation (see chart), allowing them to give friendly politicians a hand. And a tough new internal-security act was passed with minimal oversight.

This proved handy after Mr Thaksin's allies won an election in December 2007 and an inept military government was disbanded. Within months, yellow-shirted royalist protesters were back on the streets in Bangkok, refusing to leave until the government did. In the ensuing chaos, it was the army that arguably emerged on top. Urged by yellow-shirts to stage another coup, General Anupong Paochinda, the army chief, demurred. But when he refused to disperse the crowds at Bangkok's two airports last November, and instead urged the prime minister, Somchai Wongsawat, to resign,

the effect was the same.



After the mess it made in power, the army is much happier pulling the strings, says Paul Chambers of Heidelberg University in Germany. It has all the legal tools it needs to keep civilians like Mr Abhisit in line, without the bother of having actually to run the country.

Of course, General Anupong's reluctance to seize power need not preclude others from trying. Many of the 18 coups since 1932 have turned on factional rivalry within the top military ranks during the autumn shuffle of commands. But General Anupong has promoted his followers and penalised officers suspected of Thaksinite loyalties. He is due to retire next year as head of the army, the most important branch of the armed forces. His anointed successor is his deputy, General Prayuth Chan-ocha, who is young enough to serve until 2014. He is reckoned to be even more conservative than his mentor, and even readier to crack heads to defend national security and the revered monarchy. General Prayuth is likely to play a crucial role during the much-feared succession to the king, Bhumibol Adulyadej, who is 81.

Among Thais, the army commands both respect and suspicion. A recent survey by the Asia Foundation ranked it second behind the judiciary as institutions with integrity (the monarchy was not an option). But only 37% of respondents said it was neutral. Its reputation has improved since May 1992, when troops massacred scores of demonstrators in Bangkok. Never again, came the refrain. Soldiers were spat on in public. But successive civilian governments failed to overhaul the 300,000-strong armed forces. They still have several hundred active generals, many without even a desk. The tally of 36 four-star officers is just behind America's 41. But America's army is four times larger—and at war.

Mr Thaksin, who came to power in 2001, crossed the army in two ways. Firstly, he kept a lid on spending, meaning fewer fat commissions on the procurement of expensive weapons. Second, he interfered in annual promotions. Within two years he had installed his cousin as army chief. That put him at loggerheads with Prem Tinsulanonda, a retired general and former prime minister, who is the chief adviser to King Bhumibol. Assigning the most senior ranks had been the purview of Mr Prem, who chairs the Privy Council. Upstart politicians were not supposed to meddle. The resulting Prem-Thaksin feud and the 2006 coup pulled the army firmly back into politics, if indeed it had ever really left.

Asian democracies like Indonesia and South Korea have put military rule behind them, yet Thailand is swimming the other way. A civilian government with an electoral mandate might start to turn it around. But the elite in Bangkok would not tolerate another pro-Thaksin government. On September 19th the red-shirts are determined to march on the house of General Prem, the alleged mastermind of the 2006 coup. Thailand's army sees itself as the defender of the crown and suspects a republican agenda among reds. For that reason, the generals will be loth to let go until the succession is over. But repressing a mass movement in the name of a charismatic king is one thing. As Nepal's army found in 2006, doing the same for an unpopular monarch, as Thailand's crown prince would be, is a recipe for defeat.



WORLD
ASIA

Japan's new government

Poodle or Pekinese?

Sep 17th 2009 | TOKYO
From The Economist print edition

Yukio Hatoyama has to clarify some contradictory messages to the world

AFP



Hatoyama looks lost for words

THE world's leaders will have a chance at the United Nations General Assembly from September 23rd to size up Japan's new leader, Yukio Hatoyama. They will find a man flushed with having staged the most important transfer of power in Japan in more than 50 years. But what the change means for the rest of the world may well remain a tantalising mystery.

It would be odd, even disappointing, if decades of one-party rule ended without shaking up Japan's foreign policy. Its bedrock has been Japan's close alliance with America. As conqueror, the United States first demilitarised Japan, then turned it into its main Asian ally in the cold war, and then, under President Bush, encouraged it to join the "war on terror".

Throughout, American troops have been stationed in Japan, occupying 134 bases on land that is, in total, more than one-and-a-half times the size of Tokyo. For some Japanese this "footprint" is grimly reminiscent of occupation. Yet, in a region facing a growing nuclear threat from North Korea and China's inchoate deepwater fleet, American security has allowed Japan to keep defence spending around a modest 1% of GDP (it has shrunk recently). America's is four times that, and China's has soared in the past decade.

The importance of the relationship with America has spawned puzzlement and even suspicion about how Mr Hatoyama's Democratic Party of Japan (DPJ) will conduct foreign policy. In opposition, it voted against many of the security agreements with the Bush administration. It bitterly contested the Iraq war. And it has opposed the decision to spend $6 billion on relocating 8,000 marines from a base on the Japanese island of Okinawa to Guam.

Since the election, its coalition with two small parties to give it a big parliamentary majority has threatened further to strain the alliance. One of those parties consists of former socialists who have staunchly opposed keeping American troops on Japanese soil. Only after lengthy bargaining did it agree to water down its anti-American stance. For America, already frustrated with an ally whose soldiers are not allowed to shoot, all this seems alarming.

Mr Hatoyama's own muddled messages have added to the concerns. He has berated American-led "market fundamentalism", yet then called security arrangements with America the "cornerstone" of Japanese diplomatic policy. Like many Japanese, he supports global nuclear disarmament. He has pledged to investigate a supposedly secret deal allowing American nuclear-armed vessels to use Japanese ports. Yet he also wants a firm line taken against rogue North Korea.

His main foreign-policy goal is to establish a more "equal" partnership with America. This, however, puts him in the predicament of a rebellious youth desperate to break out of its parents' clutches—but unable to afford it. He has expensive campaign promises to meet, such as expanding social welfare and child support, and little scope to spend more on rearming.

The man appointed this week as foreign minister to make diplomatic harmony out of this cacophony is Katsuya Okada. He is a forward-thinking pragmatist but has little experience in government. He has expressed no desire to rock the boat with the Obama administration, which the DPJ greatly prefers to the Bush one. But he believes Japan should not automatically extend its refuelling mission in the Indian Ocean for forces fighting in Afghanistan when the agreement expires in January.

For the time being Mr Hatoyama is unlikely to provide much clarity on how he feels about the American relationship, even when he meets informally with Barack Obama at the United Nations in New York. He would far prefer to dwell on issues such as climate change, where he has already delighted environmentalists with a promise—albeit with strings attached—to cut greenhouse-gas emissions by 25% from 1990 levels by 2020.

Any changes may be more symbolic than structural. "Under the cover that Obama is not Bush, the DPJ could express a greater desire to work with the Obama administration and essentially declare a 'more equal partnership' with little substantial adjustment or cost," argue three scholars in a forthcoming article* in *Asia Policy*, an American journal.

It would be a missed opportunity, however, if Mr Hatoyama did not start to cultivate some sense that a change in ruling party means something to people outside Japan. He has appointed as finance minister a veteran fiscal hawk, 77-year-old Hirohisa Fujii, whose comments on the yen caused it to soar on September 17th. Japan's partners at the G20 summit in Pittsburgh will want to know how he plans to steer Japan's economy back to growth.

Mr Hatoyama has made a strong commitment to improve relations with other Asian countries, and has a chance of easing decades-old tensions because of his party's history of sincere apology for Japan's wartime atrocities.

Rapprochement with the neighbours, however, need not come at the cost of worsening ties with America. Throughout its history Japan, when it has not closed its doors to foreigners altogether, has tended to seek out and support the dominant or rising powers of the day, be that middle-kingdom China, Nazi Germany or post-war America. China's emergence thus presents its diplomats with something of a novelty: the task of balancing relations between two powers at once. Previous Japanese governments have struggled to define a post-cold-war foreign policy. For all the anxieties change brings, Mr Hatoyama's may be better-placed to try.

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* "Electing a New Japanese Security Policy? Examining Foreign Policy Visions within the Democratic Party of Japan", by Leif-Eric Easley, Tetsuo Kotani and Aki Mori.

Commonwealth games in Delhi

Who will bell the cat?

Sep 17th 2009 | DELHI
From The Economist print edition

India's preparations for its biggest-ever sporting event are embarrassing


Delhi 2010

WHEN is a big orange cat with black stripes, symbolic of India, not a tiger? When it's a lion, according to Lalit Bhanot, secretary-general of the Organising Committee (OC) for the Delhi 2010 Commonwealth games—for thus he describes Shera, the Games' mascot. Mr Bhanot also insists that India will be ready to host the Games, to be contested by 8,000 athletes from 71 nations in October next year. That is similarly to ignore evidence to the contrary.

India's preparations for the games are a shambles. Most visibly, 19 main sports venues are construction sites. According to a leaked report by the government's main auditor in July, work on 13 of them was badly behind schedule—with swimming, boxing, hockey and rugby sites half-finished. The main Jawaharlal Nehru stadium, built for the Asian games in 1982—India's only comparable experience of playing host to such a vast sporting event—and now being rebuilt, was never expected to stand comparison with Beijing's futuristic "Bird's Nest" stadium. But, on a visit to the site this week, it was tempting to fear it may not stand at all. The stadium's roof, to shelter 60,000 spectators, remains an aspiration. The adjoining "weightlifting auditorium" is a low-level concrete mess.

But the venues are a relatively small concern for the Commonwealth Games Federation, an anxious governing body. Its Jamaican president, Michael Fennell, wrote this month to the OC, seeking crisis talks with India's prime minister, Manmohan Singh. Mr Fennell was concerned that, with just a year to go, the committee had barely started planning to run the event. According to a leaked copy of his letter, he wanted to brief Mr Singh personally on the lack of preparations, and "seek his input in developing an appropriate recovery plan."

Such a plan might start—six years after Delhi won the games—with a serious think about transport, medical care and catering. The OC also needs to sort out ticketing. And it could use a broadcasting strategy—ideally before all the broadcasters interested in covering the event meet in Delhi next month.

Why is India, even as it demands, and gets, more respect in the world on the back of recent economic progress, making such a hash of this? It is not because it is poor. With an expected operating budget of 16 billion rupees ($335m), these games will be among the best financed ever. Nor is it because of another hackneyed excuse for inefficiency, India's democracy. The most politically contested issues, such as bulldozing slums to make way for the contestants' village, have largely been settled.

Rather, the OC displays many of the weaknesses of India's incompetent public sector at large. It is well staffed, with 300 employees. But almost every big decision is made by a small number of senior officials, including allegedly timorous and slothful bureaucrats, with no specialist understanding of their tasks—and who are therefore reluctant to make any decision at all.

The OC's deputy-boss, Randhir Singh, seems to have accepted this. "We now have to retrieve the games," he said this week. Specifically, he called for urgent changes to a system where: "There are 23 committees looking into the various organisational aspects of the games, but the chairmen of these committees hardly ever meet."

Counter-insurgency in Afghanistan

"We have too much to do"

Sep 17th 2009 | MAMKHEL, WARDAK PROVINCE
From The Economist print edition

The battle for hearts and minds in eastern Afghanistan

THE village elders were tripping over their words. "We can't help you," one protested to American troops who wanted volunteers for the armed neighbourhood watch set up to protect Mamkhel village, in Wardak province, from the Taliban. "We have too much to do. Some of us have two or three jobs at the same time."

As excuses go, it was an unlikely one, considering Afghanistan's biblical poverty. But it illustrates the difficulties the West is facing, eight years into the war, even in areas where the Taliban no longer rule openly. Wardak and neighbouring Logar province, south-west of the capital Kabul, were the first targets of America's "surge", launched in January to secure areas previously held by insurgents. Under this new strategy, troops now stay in the cleared areas to build decent local governments, protect the population and wean it away from the insurgency. Instead, Wardak has sunk into increasingly violent counter-insurgency. Attempts to win the co-operation of the area's majority Pushtuns, the ethnic base of the Taliban, have been largely futile.

American commanders do not know whether the Pushtuns are really, as they claim, too afraid of the Taliban to co-operate, or whether they in fact sympathise with the insurgents. It may be a bit of both. The Americans reckon that about 80% of the Taliban in Wardak are locals, though the ringleaders come from the south—and that most locals fight for money, rather than religion. Roshanak Wardak, a local member of parliament and a Pushtun, agrees, up to a point. "Young men here are illiterate," she says. "The Taliban tell them the Koran says they have to fight the Crusaders and they believe them."

Lieutenant-Colonel Kimo Gallahue, the commander of the American infantry in Wardak, says many locals have not yet decided which side to back. But he thinks that, given time, security, decent government and development, they would turn away from the insurgents. "It seems to me that the only people who genuinely like the Taliban are the Taliban themselves."

Perhaps. But although the Islamists no longer run Wardak, security in the province has worsened this year. The number of violent incidents has risen sixfold since January. And though the Americans have managed to secure the main north-south highway, they have been unable to push the Taliban out. "The enemy dictates the pace [of the war]," admits Lieut-Colonel Gallahue. So development efforts have gone nowhere. Of the $22m the American army has for the province, a mere $80,000 has been spent—partly because most of the money is allocated for roads, which take a long time to build.

Nationwide, the insurgents have killed over 600 Afghan civilians this year alone, according to the UN. There are hopes that this might drive some Pushtuns into the arms of the Americans, much as al-Qaeda succeeded in alienating many Iraqis. One elder in Jalrez district in Wardak offered his own sons for the neighbourhood watch after the district police chief was killed in a Taliban bomb attack in July. The sole Pushtun commander in the watch, a village leader from Jalrez, offered to patrol the district's violent areas. But to underscore the risks of co-operation, one Taliban leader who chose to lay down his arms was murdered, with his family, in his own house. Moreover, the increased violence might in fact turn the locals against the Americans, as it has done elsewhere in Afghanistan, for failing to bring peace. Roshanak Wardak, the MP, thinks foreign troops should guard the Pakistani border and leave domestic security in Afghan hands.

To some extent, this is already happening, if only because there are not enough Western soldiers. Afghan forces are increasingly active in Wardak. But most Pushtuns want nothing to do with them, especially the police. "They are worse than the Taliban," complains one man in Mamkhel. One problem is that their ethnic composition is skewed: there are few Pushtuns in the police, leaving locals distrustful.

The cavalry is not enough

More American troops may yet arrive in Afghanistan. Commanders are expected to request reinforcements in the next few weeks, even as support for the war in America has dropped to new lows. No wonder: Afghanistan is looking more and more of a shabby mess. The UN-backed electoral complaints commission has ordered a recount in 10% of the polling stations in last month's presidential election because of fraud. This may lead to a second round, something that Hamid Karzai, the incumbent, had hoped to avoid.

This week Mr Karzai was railing against election monitors from the EU, who had suggested that about 1.5m votes, a quarter of the total, might be fraudulent. According to preliminary results, the president won some 55% of the votes in the first round. If the fraud allegations were to lead to a run-off, it could take months to organise, ensuring further instability. And even if a run-off takes place, there is no guarantee the outcome would be more trusted. The Americans know they face an uphill battle to secure even the first requirement of a successful counter-insurgency campaign: a legitimate government.

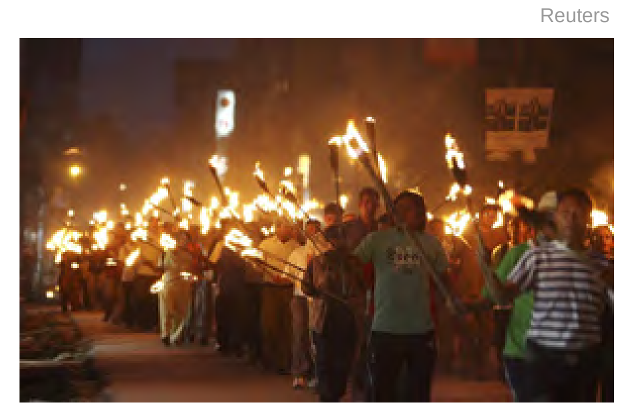
Nepal's political stalemate

Demonstration effect

Sep 17th 2009 | KATHMANDU
From The Economist print edition

Having walked out, the Maoists try to march back in

Reuters



Keeping revolutionary fires burning

LIGHTING Kathmandu with torches by night, protesters have been darkening it by day. Wherever Madhav Kumar Nepal, the prime minister, and his cabinet go, they are greeted by angry Maoists brandishing black flags. A political stand-off is worsening, threatening the fragile peace that has prevailed in Nepal since the end in 2006 of the Maoists' ten-year insurgency.

September 11th saw the biggest demonstration since May, when Pushpa Kamal Dahal (formerly known as Prachanda), the Maoist leader, resigned as prime minister and took his party into opposition. In a speech to a flag-waving crowd of about 15,000, many in red bandannas, he recalled the 40 demands he made in 2006 to the then government. Its mistake, he said, was to ignore them. Now he has 45.

The implied threat of renewed insurrection may be a bluff. But it shows how bad the Maoists' relations with Mr Nepal's ruling coalition have become. Mr Dahal had two objectives: to placate restive party activists still waiting for a revolution; and to leave room for a negotiated outcome.

The Maoists have been protesting ever since May. Mr Dahal resigned when he was thwarted in his attempt to sack the army chief, General Rookmangud Katawal, over his refusal to accept the integration of some 20,000 former Maoist fighters into the national army. General Katawal, who has since retired, was reinstated by the president. The Maoists allege this was unconstitutional and have been demanding a parliamentary debate about it.

The chances of a return to war remain slight. But Mr Nepal's fragile 22-party coalition is running out of time to find a compromise, as the Maoists, who have blockaded parliament since May, step up their protests, and demonstrate at every government event. In some districts they have begun to set up parallel local governments. This week a Maoist-affiliated trade union shut some private secondary schools across the country for four days. In Kathmandu riot police have responded to protests with bamboo sticks and tear-gas.

Having marginalised themselves, the Maoists now want to lead the government again. They won more seats than any other party in last year's elections for the constituent assembly. Many analysts believe their inclusion in government is essential for the peace process. But they are not satisfied with a partnership in the coalition, which is all Mr Nepal's ruling centre-left party has offered them so far. Mr Nepal has also accused the Maoists of trying to split both his party and the coalition. It is just possible that the Maoists will agree to join the coalition under a leader other than Mr Nepal, and that talks due as *The Economist* was going to press, between the Maoists and the two biggest parties in the ruling coalition, break the deadlock.

Despite the political stalemate, some ground has been made in recent weeks. The constituent assembly, which is supposed to write a constitution for the young republic, has managed to elect a new chairman for the main drafting committee, suspended since May. And the Maoists, who say they will not block the peace process, have agreed to sit on the committee responsible for merging the armies, which intends to complete the job in six months. But it has yet to agree on if or how the former fighters are to be integrated into the army. Until it does, and until a way is found to bring the Maoists back into government, a durable peace will remain elusive.

Economist.com



Banyan

The trials of Ah-Bian

Sep 17th 2009
From The Economist print edition

Bringing Taiwan's former president to trial is ground-breaking. A shame about the judicial flaws

Illustration by M. Morgenstern



A DRAMA that has transfixed Taiwan came to a head on September 11th when Chen Shui-bian, president from 2000 to 2008, was sentenced to life in jail for embezzlement, money-laundering and bribe-taking. A life sentence was also given to his crippled wife. This is not the end of the saga, for a long appeals process stretches ahead. Still, bringing a former leader to book is unprecedented for Taiwan. It is, indeed, an inspiring first in Chinese history for a toppled ruler to be punished by the law rather than the mob. So more's the pity that the achievement is marred by flaws in the legal system that Mr Chen's trial has highlighted.

A quick reminder of the plot to date. During the "White Terror" of the Kuomintang (KMT) dictatorship, Wu Shu-chen, a beauty from a well-to-do family, falls for the idealism of a poor tenant-farmer's son, nicknamed Ah-Bian, who has put his precocious talents as a lawyer into the fight for justice, human rights and democracy. She pays a physical price, when one day at a rally she is hit by a farm truck that runs back and forth three times over her legs. KMT hitmen may have been responsible. She is confined for life to a wheelchair.

Ah-Bian redoubles his battle against dictatorship and corruption. Opposition efforts begin to bear fruit, and democracy comes to Taiwan. In 2000 Ah-Bian himself wins the presidency as head of the Democratic Progressive Party (DPP), overturning the KMT's half-century of power. He furthers Taiwan' s democratisation, always controversially, by restructuring governing institutions and shaping a Taiwanese identity that stands out from mainland China's. But this lifetime fighter against corruption proves to be very corrupt by any standards—except possibly the past KMT's.

It has taken three years since the first real whiff of scandal for Mr Chen's followers to face up to the scale on which their man has let them down. The DPP has felt the trauma in emotional and electoral terms. As for Mr Chen's psychology, it is a story worthy of great tragedy. Friends say that high office made a humble man arrogant. They also emphasise his family's suffering. In franker moments Mr Chen confessed to abiding guilt over Miss Wu's disability. His wife seems to have played on this: didn't she deserve a few jewels the size of boulders? At heart, this has been Mr Chen's justification in his few expressions of public remorse, though former supporters think he has not apologised enough.

Yet, for all the revulsion with Mr Chen, the handling of his trial has also raised concerns. At best, many say, the judiciary has one foot stuck in the bad old days. At worst, it takes its orders from the KMT, now back in power.

The main worry has to do with Mr Chen's detention before and during the trial, including a month in solitary confinement. No one has properly explained why, after the presiding judge freed Mr Chen from pre-trial detention (to loud protests by KMT politicians), the judge was replaced. The new judge, Tsai Shou-hsun, promptly detained Mr Chen again. Mr Tsai happens to have presided over an earlier trial of Ma Ying-jeou of the KMT, now Mr Chen's successor as president, who was accused of abusing political funds when he was mayor of Taipei in ways that recall Mr Chen's case. But Mr Tsai acquitted Mr Ma, and gave an aide involved in the abuse a year in jail.

Mr Chen's supporters, pointing to his life sentence, and to the 20- and 16-year sentences meted out respectively to two of his aides, claim a political vendetta by the KMT, orchestrated by Mr Ma. That would hardly be in keeping with the clean-guy image of Mr Ma, a Harvard-trained lawyer. It would also throw into question how far Taiwan has really come as a law-based democracy. But it is more plausible to blame the trial's flaws on a legal system that has only imperfectly made the leap from being venal and biddable under dictatorship towards judicial independence and due process. Six years ago Taiwan's judge-prosecutors were replaced by a system in which impartial judges are meant to hear out the case for the prosecution and the defence. Mr Tsai's open hostility to Mr Chen during the trial suggests some old-school attitudes are hard to shake off.

What is more, prosecutors' immense powers, including the practice of interrogating an individual without letting him know what he is said to have done, remain a blot on democracy. Shameful too was the skit performed at the prosecutors' annual dinner in which mockery was made of Mr Chen famously protesting at the humiliation of having to wear handcuffs. No rebuke came from the government. Now the justice ministry threatens to disbar Mr Chen's lawyer, Cheng Wen-lung, for questioning the fairness of the judicial process. That smacks, says Jerome Cohen, Mr Ma's former law professor, now at New York University, of the persecution of human-rights lawyers in China.

Drawing the right conclusions

What conclusions you draw about the future rule of law in Taiwan depend on whether you believe Mr Chen' s trial was politically motivated or not. If not—and the investigation of Mr Chen, after all, began when he was still president—then the trial of a former president is surely a landmark. What is more, the legal system is responding to the trial's shortcomings. For instance, thanks to a challenge by Mr Chen, the prosecutors' insistence that they attend and record meetings between defendants and their counsel has now been ruled unconstitutional.

More telling, the KMT is looking anew at the whole business of murky political funds which the reforming Mr Chen should have addressed as a cancer on democracy, but instead dipped into. And most telling of all is China's official reaction to the downfall of an enemy loathed for his embrace of Taiwanese independence. The reaction has been very nearly mute. After all, to cheer Taiwan's pursuit of a corrupt leader might encourage China's own citizens to draw all the wrong inferences about what should happen to their own rulers.

The UN report on Israel and Gaza

Israel in the dock

Sep 17th 2009 | JERUSALEM
From The Economist print edition

A report by a UN body controversially chastises Israel's government and its army for their actions during the war in Gaza earlier this year

AP



EVER since Israel's intense, three-week war in Gaza ended in January, its politicians and soldiers have been carpet-bombed by critical reports, both foreign and Israeli. These have taken aim at the conduct of the operation, some of the weapons used, many of the targets chosen, and the behaviour of some members of the Israel Defence Forces (IDF). For a country that prides itself on having "the most moral army in the world", the accusations, though mostly rejected, have stung.

But even the most battle-hardened officials were shocked, then furious, at the litany of accusations in a 575-page report published this week by a fact-finding mission headed by Richard Goldstone, an eminent jurist. The incendiary premise of his report, to be delivered to the UN's 47-country Human Rights Council in Geneva this month, is that Israel is guilty of one of the worst crimes: deliberately and systematically attacking civilians and making them suffer as a war aim. The Israelis knew they would get pasted, as the council is a serial Israel-bashing outfit that often lets more egregious human-rights abusers around the world off the hook. But the report was even more critical than they had feared.

Just as damning in Israel's eyes is its claim to find little or no evidence that Hamas, an Islamist Palestinian group that controls the densely populated Gaza Strip while refusing to recognise Israel, deliberately fired rockets from civilian houses, stored weapons in mosques and used the basement of one of Gaza's main hospitals as a military command centre. If Hamas did such things, says Mr Goldstone, they might be judged war crimes too.

The report claims that Israel specifically sought to punish Gaza's civilians because many of them back Hamas, which won a general election in 2006 in the Palestinian territories, including the separate but bigger West Bank. A year later, in Gaza, Hamas violently ousted Fatah, its secular rival that had long ruled the Palestinian roost.

Israel, which refused to co-operate with the UN mission, flatly denies it sought to hammer civilians. Its aim, it says, was to stop Hamas firing rockets, with increasing range, at towns in southern Israel. Since late 2004, they had killed 16 Israeli civilians and injured many more, terrified thousands of them, and disrupted the economy. Mr Goldstone's report criticised the indiscriminate firing of rockets as potential war crimes, but concentrated overwhelmingly on Israel's shortcomings. President Shimon Peres remarked that the authors "would not have written those things if their children lived in Sderot [a southern Israeli town

close to Gaza], under the threat of constant rocket attacks”.

The number of civilian deaths in the Gaza war is disputed. B’Tselem, an Israeli human-rights monitor, puts the figure at more than 770; the Israeli government says much fewer. Various international outfits put the overall death toll at more than 1,400; the Israeli government says 1,166.

In any event, an interim report issued by Israel’s government in July listed measures it said it had taken to keep the civilian toll as low as possible. It had aborted air strikes when the risk to civilians was too great, dropped warning leaflets and made telephone calls to Gazans, and declared daily humanitarian pauses in the fighting.

Indeed, the Israelis point out that even as fighting raged, some Palestinians were able to complain about humanitarian issues directly to Israel’s Supreme Court for immediate ruling. Legal advisers, involved in planning the operation from the start, were deployed during the fighting round the clock. Israel offers this as evidence of good-faith efforts to minimise civilian harm. The Goldstone report cites it as evidence of crimes deliberately committed.

The report accused the IDF, among other things, of recklessly using white phosphorus and of attacking police stations, civilian ministries, food-producing factories, sewage plants and electricity stations. The Israelis retort that white phosphorus is legally used by many armies as a smokescreen provided it is not fired over densely populated areas. And it says that Hamas, a terrorist movement, makes little distinction between security and civilian matters. The Israelis’ own report acknowledges mistakes made by all armies in the fog of war: some wrong buildings hit, cases of misidentification of civilians as fighters.

Few if any conflicts have been subject to this level of forensic investigation. Some allegations of wrongdoing by individual soldiers have been raised by lobbies such Human Rights Watch, a New York-based group, and Breaking the Silence, an Israeli outfit set up by former soldiers to educate the public in the grim realities of occupation on the West Bank. Official Israeli investigators are looking into upwards of 100 Gaza-related complaints; 23 criminal investigations have been opened so far.

Mr Goldstone’s daughter, Nicole, who lived in Israel for many years but now lives in Canada, vigorously defended her father’s report in an interview on the army radio. “If it hadn’t been for him, the report would have been even harsher,” she said, speaking in Hebrew. But for Mr Peres the Goldstone report makes “a mockery of history, by not distinguishing between the aggressor and the defender…Any other country would have done the same.”

Iran's shaky government

Not over yet

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From The Economist print edition

Three months after his disputed re-election, Iran's president, Mahmoud Ahmadinejad, is still failing to reassert his—and his government's—grip

Reuters

More prayerful than beady

THOUGH it has crushed street protests, jailed dissidents, mounted show trials and hardened censorship, Iran's ultraconservative, military-backed government remains shaky as it faces a string of testing challenges, including a looming diplomatic showdown over its nuclear ambitions. For sure, it has a physical hold on the Islamic Republic. Its increasingly militarised look, its uninhibited resort to coercion, its domination of parliament and the state-controlled press, and the tacit approval all this gets from Iran's supreme leader, Ayatollah Ali Khamenei, show its determination to prevail at any cost. But opposition has not faded. Not only do the two defeated reformist presidential candidates still insist they were cheated, but other powerful figures, including top clerics, persist in decrying the abuse of human rights.

A recent blast came from Hosein Ali Montazeri, a grand ayatollah, now 87, once tipped to succeed the Islamic Republic's founding father, Ayatollah Ruhollah Khomeini, as supreme leader. Expressing deep shame in a widely disseminated letter, he called on fellow clergymen to denounce the government so as to preserve the reputation of Islam. In an apparent response, police in the Shia seminary city of Qom detained three of his grandsons, along with relatives of other dissident clerics.

A lot of ordinary Iranians, including many who used to back the conservatives, scorn Mr Ahmadinejad's claim to have foiled a foreign plot. Instead, they have added charges of the rape, murder and slander of its opponents to the regime's alleged initial sin of massive voting fraud in the June election. Some argue that the scale and brutality of the regime's crackdown reflect not strength but desperation. With internet and satellite airwaves still evading state control, large-scale unrest could yet erupt, particularly when the fasting month of Ramadan ends and the school year begins.

A first test looms on September 18th, which the Islamic Republic has long celebrated as Jerusalem Day, an occasion intended to show Muslim solidarity with the Palestinians. Opposition leaders have already appropriated such Islamic symbols as the colour green and the cry of "Allahu Akbar!" Now they have called for a huge turnout on Jerusalem Day, vowing to attend the event themselves. Rather than small pro-government crowds chanting "Death to Israel!", this year's protest may look more like the vast shows of people-power sparked by June's election result, with the anger directed at Iran's own rulers rather than distant Zionist oppressors.

Such worries have already prompted Mr Ahmadinejad to cancel several public observances, an unusual step in the anniversary-obsessed Islamic Republic. Jerusalem Day is too big an event to scrap. Instead, the government has blocked Akbar Hashemi Rafsanjani, a wealthy former president who is one of the remaining bulwarks against the conservatives, from delivering the main address in Tehran, Iran's capital, as he has done for the past 20 years. Mr Ahmadinejad himself will introduce a hardline loyalist cleric as the speaker. The state-run media will surely then attempt to portray any large crowd as supporting the government. Yet given the sullen, restless mood in Tehran, it is unsure whether such tactics will prevent an embarrassing public-relations flop. In July crowds pointedly substituted Russia for America in the "death to" catechism.

This could hurt Mr Ahmadinejad as he embarks on the first important foreign tour of his second term. Next week he is to join a host of leaders in New York, where he will address the UN General Assembly shortly after America's president, Barack Obama. Mr Ahmadinejad may eschew the inflammatory talk that prompted a walkout at a UN gathering last year in Geneva. But Iran's diplomatic isolation will be exposed on September 24th, when Mr Obama is to chair a Security Council summit on nuclear proliferation.

American diplomats, keen to help Mr Obama in his stated intention to engage Iran, have been careful to portray the Security Council's agenda as broad—and targeted at no particular country. A part of an American draft resolution, for instance, calls for nuclear-armed states to vow never to use such weapons against non-nuclear states. But reports suggest it will include language that would more closely tie the right of countries to develop peaceful nuclear technology to their strict adherence to the Nuclear Non-Proliferation Treaty.

Iran has long insisted that its plans are peaceful, and so within its rights, but others have frequently charged it with violating the treaty. The new wording is meant to rally hitherto reluctant Security Council members, such as Russia and China, behind a stiffening of the economic sanctions imposed on Iran in 2006, after it refused to obey a demand by the International Atomic Energy Agency, the UN's nuclear watchdog, to suspend the enrichment of uranium. The aim is to make Iran more co-operative at multilateral talks due to start on October 1st, probably in Turkey.

That much-anticipated meeting will confront Iran's chief nuclear negotiator with representatives of the UN Security Council's five permanent members plus Germany. Earlier this month Iran countered the so-called P5+1 group's longstanding demand for talks with a flowery proposal for broad strategic negotiations that would bury the nuclear issue. But since Mr Obama dropped his predecessor's more-stick-than-carrot approach, the big-power enforcers may let the Islamic Republic pose as having won respect for its nuclear rights. Such diplomatic forbearance may not endure for long, if Mr Ahmadinejad shows the same disregard for world opinion as he does for his own voters.

Riots in Uganda

In whose interest?

Sep 17th 2009 | KAMPALA
From The Economist print edition

Museveni, Qaddafi and the mysterious protests

AFP



Long live our king!

RIOTS rocked Kampala in support of the king of the Baganda, the country's largest ethnic group. Shops in the capital were looted, cars burned. Uganda's president, Yoweri Museveni, who hails from the much smaller Ankole group, ordered police and soldiers onto the streets. At least 24 people were killed in and around the city; most were shot. The government says the rioters themselves had guns. In fact, it seems likely that the armed forces fired into the crowds. The main Bagandan radio station was closed. Some journalists were arrested and charged with sedition.

Events would have spun further out of control had the Bagandan king, or *kabaka*, Ronald Mutebi, not cancelled a planned trip to the north of the city. Mr Museveni's aides told the *kabaka* he would be held responsible for further bloodshed. So he was kept in his palace. Many of his people were enraged by this apparent humiliation.

Buganda is the largest of Uganda's five ancient kingdoms banned under the presidencies of Milton Obote and Idi Amin but revived by Mr Museveni. The Baganda make up 17% of Ugandans. They are not generally averse to Mr Museveni and his political party, the National Resistance Movement (NRM). A majority of them voted for him in the last election, in 2006. The vice-president and numerous ministers and MPs are Baganda, along with many civil servants doing the NRM's bidding. So why are Mr Museveni and the Baganda now at loggerheads, especially as the president is seeking re-election in 2011?

Mr Museveni thinks the Baganda have been getting uppity. Though their kingdom is the largest and was once the most powerful, it is now a ghostly fiction, with no sovereignty and little wealth. Mr Museveni is especially weary of persistent Bagandan demands for a return of a swathe of claimed ancestral lands that were long ago distributed to pastoralists or pilfered by officials—and are most unlikely ever to be given back. Besides, generosity to Buganda would aggravate the other kingdoms, particularly neighbouring Bunyoro, whose land includes Uganda's new-found oilfields.

Mr Museveni may calculate that he can treat the Baganda harshly now, but retain their votes by granting them concessions nearer the election. He has been adept at dividing and conquering the electorate, using carrots and sticks. He dishes out jobs to loyalists but harasses businessmen suspected of helping the fractured opposition. He says he will limit the *kabaka*'s power and chastises "meddlers" harming Uganda's prospects.

Mr Museveni's people say they have identified another villain of the piece: Libya's president, Muammar Qaddafi, whom they accuse of giving cash to the Baganda. For several years Mr Qaddafi has subsidised Uganda's kings and their cultural institutions as part of an exotic plan to unify Africa in a web of chiefs and

kings. But his latest dollops of cash, say Mr Museveni's friends, were meant to stir up trouble, because Mr Qaddafi has fallen out with Mr Museveni, despite helping him to win a bush war that brought him to power two decades ago.

Mr Museveni has ridiculed Mr Qaddafi's swaggering "king of kings" approach, preferring to build up Africa with regional trade blocs such as the East African Community. Still, it is odd that Mr Qaddafi should want to poke Mr Museveni in the eye by funding riots, since the recent oil discoveries in Uganda should make its president more attractive as a friend. Libya, for instance, hopes to tender for a big oil refinery that Mr Museveni wants to build.

Zimbabwe's land invasions

Out with those white farmers

Sep 17th 2009 | CHEGUTU AND JOHANNESBURG
From The Economist print edition

President Robert Mugabe is still bent on chasing out the last white farmers

Eyevine



Ben Freeth's reward for staying put

FOR Mike Campbell and Ben Freeth, his son-in-law, leaders of a legal battle to save Zimbabwe's last white-owned farms, Robert Mugabe's warning came too late. By the time the president made his latest tirade against white "imperialist" farmers, their own farmsteads were no more than a pile of ashes and rubble. And just days after the arson attacks, two mysterious explosions shook the farm. On September 14th the police, who say they are now investigating a suspected arms cache, briefly arrested Mr Freeth and held a visiting crew from the al-Jazeera television channel for "entering a potential crime scene".

The arms-cache trick has been played before, on Roy Bennett among others. He is a dispossessed white farmer who was appointed deputy agriculture minister in the power-sharing government set up in February with Morgan Tsvangirai, the former opposition leader, as prime minister. In 2006 Mr Bennett was charged with treason after the discovery of an arms cache at an alleged co-conspirator's home. The treason charge, which carries the death penalty, has since been dropped. But Mr Bennett is still facing trial on equally spurious terrorism charges next month. Mr Mugabe still refuses to let him be sworn in as a minister.

Since the land seizures began a decade ago, some 4,000 owners (virtually all white) of Zimbabwe's most productive farms have been forced out, along with their 320,000 workers (almost all black) and their families, amounting to 1m-2m people. Although around two-thirds of the land has been allocated to 140,000 poor black families, the rest has gone to Mr Mugabe's relatives and comrades, most of whom have little or no interest in farming. Vast tracts of fertile farmland now lie fallow; agricultural output has slumped. One of Africa's biggest food exporters is now one of its main recipients of food aid.

Of 6,500 white commercial farmers in 1980, when Mr Mugabe came to power, only about 500 remain. But it is clear from the treatment meted out to Messrs Campbell and Freeth that Mr Mugabe wants the whole lot out. In a speech on September 11th, on the eve of the European Union's first high-level visit to Zimbabwe in seven years, he called on his ruling Zanu-PF party's youth wing to "protect" their God-given land from the designs of new white imperialists and told the "former" commercial farmers to abandon their uneven struggle. Once the government had issued an "offer letter", supposedly giving the recipient the right to take over a designated white farm, "that's it," he said. "The farm is not yours any more. Please don't resist."

For Mike Campbell and Ben Freeth, their own saga began in 2004 when Nathan Shamuyarira, then Mr Mugabe's information minister, turned up one Sunday at lunch time at their 1,200-hectare Mount Carmel Farm in Chegutu, a couple of hours' drive south-west of the capital, Harare. He announced he had been given the right to take over what was then Zimbabwe's biggest mango farm. Mr Freeth insisted that the minister first go through the correct legal procedures.

It was a bold, perhaps foolhardy, reaction. Thirteen white farmers had by then been murdered and dozens more beaten up or jailed for resisting the seizure of their farms. Though no one in the Campbell-Freeth families has been killed, they and their 150 workers have, over the past five years, been subjected to repeated harassment and terrifying intimidation.

On one occasion, 15 armed invaders, banging on metal objects and chanting war songs, forced their way into Mr Freeth's house, threatening to burn it to the ground, kill the two men present, rape the women and eat the three children asleep in their beds. Thanks to an earlier beating, Mr Freeth, an emaciated,

soft-spoken man of 40, has never recovered his sense of smell. Mr Campbell, 76, was so badly thrashed that his memory is impaired.

The invaders, who say they are acting on behalf of Mr Shamuyarira, though he has not been seen at the farm since his first visit five years ago, have taken the Campbells' home and their entire farm, leaving most of the crops to rot in the fields. Like many of the other remaining white farmers, Mr Freeth has turned to God. He has already started rebuilding his house. He says he is determined to stay.

Last November, in a case brought by Mr Campbell on behalf of 77 other white farmers, a tribunal of the Southern African Development Community (SADC), a 15-member regional group that includes Zimbabwe, ruled that all land seizures since 2000 were discriminatory and violated both domestic and SADC treaty law. Mr Mugabe and his ZANU-PF ministers claim that the tribunal has no legal standing. In a further violation of the tribunal's ruling, around 170 white farmers are now being prosecuted in Zimbabwe's courts for refusing to leave their land.

In June the tribunal held Zimbabwe to be in contempt of court for failing to enforce its earlier ruling and asked SADC to take up the matter urgently. But at the group's summit earlier this month, no mention was made of this or any of the other matters bedevilling Mr Mugabe's seven-month-old power-sharing arrangement with Mr Tsvangirai. It was a stunning victory for the 85-year-old president.

Mr Tsvangirai is in a quandary. In a speech this week, he promised to stand by the farmers. Yet he has blown hot and cold on the issue since he became prime minister. At first he said that not a single crime against white farmers would go unpunished, though no prosecutions have ever been brought. He has also claimed that the issue has been "blown out of proportion" by the press. In any event, Western donors have so far been firm. Unless farm invasions stop—and the likes of Messrs Campbell and Freeth are treated fairly—development aid will not resume.

Al-Qaeda in Somalia

The long arm of America

Sep 17th 2009 | NAIROBI
From The Economist print edition

In a foray into Somalia, American special forces claim to hit a prize target



IN THE past few years America has occasionally attacked suspected jihadist enemies lurking in the ungovernable badlands of Somalia. Two years ago it killed Abu Talha al-Sudani, a Sudanese explosives expert linked to al-Qaeda, who was suspected of helping to blow up the American embassies in Kenya and Tanzania in 1998. More recently American missiles have rained down on the footsoldiers of Somalia's Shabab ("Youth") militia, an Islamist group that looks to al-Qaeda for inspiration and material support and which has overrun swathes of Somalia. This week America made its most brazen and daring foray into Somalia since the early 1990s, reportedly killing Saleh Ali Nabhan, a Kenyan of Yemeni descent, who had been suspected of an al-Qaeda attack on a hotel in the Kenyan port of Mombasa in 2002.

The American commandos flew in daylight in helicopters from a naval ship off Somalia's coast, attacking Mr Nabhan and a score of other foreign and Somali fighters as they drove in two lorries across the desert. Mr Nabhan's body was zipped up with body parts of other fighters and taken to a freezer on the ship for DNA analysis.

Barack Obama's administration evidently decided that the risk of putting American soldiers on the ground in Somalia, albeit briefly, was worth taking. Specialists working for a unit that collects the DNA of suspected terrorists had argued that previous missile attacks on targets in Somalia ordered by George Bush's administration had so mangled those killed that it was hard to identify the bodies after the event. Moreover, missile attacks invariably kill civilians as well as jihadists, making it easier for the Shabab to rally locals to their banner.

It is uncertain whether Mr Nabhan was, as the Americans claim, an actual link between the Shabab and al-Qaeda in Pakistan. But the manner of the raid and the quality of the intelligence that pinpointed him may dent the Shabab's aura of invincibility. In return, Somalia's jihadists may try to exact revenge. As they scuttle into the mangrove swamps and the desert, their leaders promise to hit back at Western targets. A French security agent and other foreigners held hostage by the Shabab may be at risk. And some experts fear the Shabab may try to carry out suicide-attacks in Kenya or Ethiopia, where the governments continue to let the Americans use their territory for counter-terrorism.

Russia's political leaders

Behind the golden doors

Sep 17th 2009 | MOSCOW
From The Economist print edition

President Dmitry Medvedev sets out a modernisation agenda, but he may yet be undercut by his prime minister, Vladimir Putin

Getty Images



SOMETIMES you have to admire the candour of Russian leaders. Whereas Kremlinologists love conspiracy theories, Dmitry Medvedev, Russia's president, and Vladimir Putin, its prime minister, tell things how they are.

On September 10th Mr Medvedev published a manifesto on gazeta.ru, a Russian website, highlighting Russia's failings. He wrote of a primitive, oil-dependent economy, weak democracy, a shrinking population, an explosive north Caucasus and all-pervasive corruption. His critics would not disagree with this stark diagnosis, even if he offered few answers. A day later Mr Putin told the visiting Valdai club of foreign journalists and academics that he and Mr Medvedev would decide between themselves who is going to be president when Mr Medvedev's first term expires in 2012 (see article). Most Russians already assumed as much.

One subject both leaders avoided was how this tallies with Mr Medvedev's lament about the weakness of democracy. Nor do they explain what they have been doing in their past ten years in charge. Mr Medvedev's article reads like a cry of desperation, an attempt to appeal to Russian progressives over the heads of corrupt bureaucrats. "The global economic crisis has shown that our affairs are far from being in the best state. Twenty years of tumultuous change has not spared our country from its humiliating dependence on raw materials," he notes. He predicts optimistically that Russia will develop a knowledge-based economy and lead the way in new technologies, which may in time lead to an open and flexible political system that fits the requirements of a free, prosperous and confident people.

In politics, however, Mr Medvedev is more cautious. "Not everyone is satisfied with the pace at which we are moving in this direction. They talk about the need to accelerate changes in the political system. We will not rush." He ends with a dramatic flourish. "Influential groups of corrupt officials and do-nothing entrepreneurs are well ensconced. They have everything and are satisfied…But the future does not belong to them—it belongs to us. And we are an absolute majority."

Mr Medvedev's article evoked memories of Mikhail Gorbachev's *perestroika* speeches in the 1980s; he said this week that what went wrong with Mr Gorbachev was that he began but failed to complete his reforms. Mr Medvedev, however, has not ever started. But cynics also saw an echo of Mr Putin's first state-of-the-nation address as president in July 2000. Mr Putin talked then of a shrinking population, a backward

economy and the importance of freedom of speech and human rights.

So it is not surprising that many Russians were unimpressed. As one website visitor commented: "Mr President, your mostly correct words have *nothing* in common with what is happening in the country of which you are the leader. I don't believe you. Do something first, something that would illustrate your readiness to modernise the country and move it forward. Fire the government or let Khodorkovsky out. At least do something!"

The problem, argues Nikolai Petrov of the Carnegie Moscow Centre, is that the economy cannot become dynamic and progressive if the political system is not fair and free. But Mr Medvedev's liberalism is virtual not real. In 18 months of his presidency, the Russian media has not become any freer. Political opponents have not gained access to television. The number of murders and attacks on human-rights activists has gone up. And the trial of Mikhail Khodorkovsky, once one of the country's wealthiest oligarchs, has turned into a showpiece of political repression.

Mr Medvedev's article and Mr Putin's comments on 2012 may reflect a tension between the two men and their teams that has brought Russia into a state of inactivity caused by competing forces. Stasis is certainly visible in Mr Khodorkovsky's trial. In what looks like the theatre of the absurd, prosecutors have for weeks been senselessly reading out pages from their multi-volume case, often confusing pages and repeating passages twice. Their aim seems to be to drag out the case while the powers-that-be decide what to do.

In the past few months some of Mr Medvedev's supporters have defected to Mr Putin's camp, arguing that modernisation is possible under the prime minister's leadership. Others, such as Gleb Pavlovsky, a weathered Kremlin spin-doctor, have been trumpeting Mr Medvedev's emergence as an independent and powerful leader. Mr Medvedev's new-found ambition may also have been boosted by Barack Obama. The American president went out of his way during his July visit to treat Mr Medvedev as the real leader. Mr Medvedev talked to the Valdai club about the joys of spending eight hours with Mr Obama, whereas Mr Putin reminisced more about his old friend George.

Mr Putin's words about 2012 undermine Mr Medvedev, making him a lame duck 30 months before his term runs out. Mr Medvedev has spent most of his career as Mr Putin's subordinate. It was his loyalty, not his independence, that qualified him for the top job. As president he has largely followed Mr Putin's policies, including in last year's war with Georgia. He visited South Ossetia and introduced a new law that makes it easier to deploy Russian forces outside the country. And it was Mr Medvedev who sent an aggressive and insulting letter to Viktor Yushchenko, Ukraine's president, blaming him for supplying arms to Georgia and falsifying history.

Indeed, January's presidential election in Ukraine may be the key event in Russia's new political season. Five years ago Mr Putin suffered the biggest embarrassment of his presidency when he rushed prematurely to congratulate Viktor Yanukovich as winner, only to see him pushed aside in the "orange" revolution. The election offers him an opportunity for revenge. Gazprom, Russia's gas giant, is already muttering belligerently that Ukraine may be unable to pay its gas bill after the vote.

As Mr Medvedev's letter to Mr Yushchenko shows, he fits in with the Kremlin's policy of confrontation and the search for enemies, particularly at times of crisis. The tension at the top of the government does not seem to make Russia any friendlier towards the West. Although his article said that Russian foreign policy should be defined by the goal of modernisation, Mr Medvedev shook hands with Venezuela's Hugo Chávez on an arms deal (see article). "We will supply Venezuela with the types of arms it asks for, acting in compliance with our international obligations. We will certainly deliver tanks too, why not? We have good tanks."

On September 14th, at a conference on global security in Yaroslavl, Mr Medvedev again lambasted America for causing the global crisis. He also called for a new European security architecture that would give Russia greater influence, particularly in the former Soviet space. For the moment, though, European and American security experts are more interested in another matter: what cargo a Russian vessel, *Arctic Sea*, was carrying when it vanished in closely monitored European waters, why a journalist who alerted the world to its disappearance had to flee Russia and why Binyamin Netanyahu, Israel's prime minister, paid an urgent and secret visit to Moscow just a few days later. True to form, Mr Medvedev's article gives no answers to any of these questions.

Russia's odd couple

The Vladimir and Dmitry show

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Vladimir Putin prepares the stage for his re-entry

TO SEE Russia's two leaders in quick succession is instructive. The more so if the issue is which should run for president in 2012, when Dmitry Medvedev's current term expires. Vladimir Putin, tanned and muscular, positively twinkled as he told the Valdai club of foreign academics and commentators over lunch on September 11th that "we will reach an agreement. We understand each other. We are people of one blood, with the same political views…We will look at economic and political factors, and at the position of the United Russia party, which I head, and then decide."

It had long been rumoured that Mr Putin, now prime minister, might want to return as president. In 2008 he chose not to amend the constitution, which bars more than two consecutive terms, but instead gave the job to Mr Medvedev. Under Mr Medvedev, the terms were extended from four to six years.

The response from Mr Medvedev was woollier than the barbed (and carefully prepared) words of Mr Putin. At another lunch with the same group on September 15th, the suave if somewhat bloodless president first made a lame joke about blood groups. Then he mused "How am I to answer this question?…Some time ago I didn't want to run for the presidency, but fate has intervened, so I am not making any forecasts for myself." But he added that he was not ruling anything out. The possibility that he might not run again had been hinted at already by his main economic adviser, Arkady Dvorkovich, who said at yet another lunch that he had two-and-a-half years left to implement reforms.

That there are tensions between the two political leaders was suggested not just by the jousting over 2012. Mr Medvedev also pointedly said that he saw and spoke to Mr Putin "less than some people think—maybe once a week." And Mr Putin himself drew an analogy with Britain's Tony Blair and Gordon Brown, noting caustically that "when my friend Tony Blair retired, Gordon Brown immediately became prime minister. Did the British people participate in this? No." He may have missed the irony that Mr Blair and Mr Brown were a famously dysfunctional pair in British politics.

It seems clear that it will be Mr Putin, not Mr Medvedev, who will take the final decision. And if he does run in 2012, he may do so again in 2018, serving until 2024. That might seem an eternity, but Mr Putin would be only just over 70—younger than his good friend Silvio Berlusconi, the prime minister of Italy, is today.

France's carbon tax

Taming the carbonivores

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Hot air over a tentative carbon tax

FRANCE'S president, Nicolas Sarkozy, does not like to do things by halves. In characteristically grandiose fashion he described his plan to introduce a carbon tax as "the only choice that could guarantee…the future of our planet". If it goes ahead, France would be the first big country to adopt such a tax, which exists in Scandinavia. But the proposal has already run into fierce hostility, from consumers, opposition parties—and even greens.

AP



Tooled up for Copenhagen

Mr Sarkozy plans to bring in his carbon tax in January next year. It will be levied at a rate of €17 ($25) per tonne of carbon dioxide emissions, a bit higher than Denmark's rate, though a lot less than Sweden's. This translates into roughly an extra four cents a litre of petrol at the pump. It will apply to the consumption of petrol, gas and coal, but not to electricity, on the ground that France generates 80% of its electricity from almost carbon-free nuclear power.

The idea is to try to discourage "carbonivorous" behaviour, rather than to fill depleted government coffers. So the tax is supposed to be fiscally neutral. The government says it will compensate households through an income-tax deduction, worth €112 per year for a family with two children living in a town. Country folk, lacking public transport, will get a bit more back. Those who do not pay income tax will get a "green cheque" instead. Companies will be compensated by the reform of municipal corporate tax.

Although the French have become increasingly green-minded, with plastic bags disappearing from supermarket checkouts and regular recycling collections, Mr Sarkozy's plans have prompted a political outcry. Ségolène Royal, the defeated Socialist presidential candidate, denounced the tax as "unfair" because it affects the rich and the poor alike. Greens, in contrast, grumbled that it was not bold enough. Greenpeace, an environmental lobby group, said "it would change absolutely nothing in terms of behaviour."

In truth, some of this hostility is due less to anti-greenery than to anti-Sarkozy posturing. Ever since a coalition of ecologists nearly beat the Socialists into third place at the European elections in June, French political parties have been wrangling over the environment, each claiming to be greener than the other. Mr Sarkozy himself is a relatively recent convert. A book that he wrote a year before the 2007 presidential election, intended as a draft manifesto, contained barely a word on the subject. By the time of his campaign, however, he had become a studied tree-hugger. Now, ahead of the international climate-change conference in Copenhagen in December, he wants to show that France is taking the lead.

Mr Sarkozy will probably get his carbon tax through parliament without too much difficulty. He has a large majority and public opinion may be less hostile than some of his critics suggest. When asked by CSA, a polling agency, if they wanted a carbon tax, 74% of respondents were against. However, when asked if they would back such a tax if it were fiscally neutral for households, 52% were in favour.

The harder question is whether France's carbon tax will live up to its billing. Mr Sarkozy says he will now push for a Europe-wide carbon tax on imports from countries that "do not respect any environmental or social rules". That leads some to suspect that his ultimate objective is to create a pretext for protectionism.

As it is, Mr Sarkozy's carbon tax has many exemptions. Heavy industry will not pay, on the ground that it is already contributing through Europe's cap-and-trade system. Fishermen and farmers, who anyway pay far less tax on fuel than ordinary French consumers, will get special compensation. Moreover, by not

taxing electricity at all, the government is sending a somewhat mixed message about what constitutes good green behaviour. In many ways, Mr Sarkozy's new tax is more of a fuel tax than a real carbon tax.

As an incentive to change behaviour, the tax rate also looks too low. Who will keep the car in the garage just because of an extra four cents a litre on petrol? Sweden's carbon tax is levied at fully €108 per tonne of CO2, over six times the French rate. Earlier this year, an official carbon-tax commission, headed by Michel Rocard, a Socialist former prime minister, proposed a rate of €32, arguing that anything less would not change habits.

Mr Sarkozy says that he will increase the tax rate in time. Indeed, this is what Sweden did, having started in 1991 with a lower carbon-tax rate of €26. "The truth is that if you start too high, you'll never get it through," says Dieter Helm, an environmental economist at Oxford University in Britain. "You can always raise it later." Until then, a far greater incentive to reduce fuel consumption may turn out to be a quite separate plan—expected to be unveiled next week—for a generous cash subsidy to buy electric cars.

Norway's election

Rich but worried

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From The Economist print edition

Jens Stoltenberg is popular, but his government is less so

AP



Vote for Jens, vote for the EU?

IN MOST countries, a charismatic leader who guided the nation more or less unscathed through the worst economic crisis in eight decades should be a sure bet for re-election. Not in Norway, where Jens Stoltenberg's centre-left coalition this week barely scraped back into office with a reduced majority.

It secured 86 seats in the 169-seat Storting, one fewer than it won four years ago and just one more than the 85 required for a majority. The problem is hardly Mr Stoltenberg himself: his Labour Party, the largest in the coalition, won an extra three seats. A clever, affable outdoorsy type given to scuba diving, hunting and hiking, he ranks high in popularity polls.

The economy is in good shape too. The unemployment rate, at 3%, is the lowest in Europe. Norway has bounced back from the mild recession it suffered in the early months of this year. It is expected to grow by around 2% next year. The $400 billion wealth fund that holds surplus revenues from North Sea oil and gas exports, turning petrodollars into a hoard of stocks and bonds, naturally took a hit in the market slump but is still worth some $85,000 per citizen.

And the Norwegians themselves seem a largely content bunch. Why wouldn't they? A stroll through Bergen, Norway's second city, reveals handsome, well-fed citizens who work in designer offices or high-tech fishing vessels, relax in art galleries and theatres, and enjoy pristine scenery. Education is free and health care is heavily subsidised.

"Norway is not perfect," concedes Mr Stoltenberg, explaining that perceptions of social injustice are relative and that jobless Norwegians measure themselves against a high general standard of living. This perhaps explains the appeal of Siv Jensen's populist right-wing Progress Party, which rose from 38 to 41 seats. Her message that Norway has the money both to boost public services and to cut taxes struck a chord with voters, though not enough to secure victory. The defection of voters from smaller parties gave the centrist Conservatives an impressive seven extra seats.

Mr Stoltenberg's next task is to draw up a new coalition pact and a budget for 2010. Two rows are brewing within the coalition. The prime minister seems to favour oil exploration around the pristine Lofoten archipelago in the Arctic, but this is opposed by the Socialist Left. And he wants Norway to join the European Union—particularly if Iceland succeeds in its quest for membership.

Charlemagne

In knots over headscarves

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From The Economist print edition

Antwerp's cautionary tale about the complexities of educating Europe's Muslim children

Illustration by Peter Schrank



FOR all its grand central squares and lively cultural scene, the Belgian port of Antwerp is not always a happy town. Flemish old-timers share its gritty streets with Arabs, Africans, Asians and, in the diamond district, Hasidic Jews. Race relations are not easy: in the latest local elections, a third of the vote went to Vlaams Belang, an anti-immigrant, far-right Flemish nationalist party. The handsome stone bulk of the Royal Atheneum, a once-elite state school with a 200-year history, has produced legendary free-thinkers and radicals in its day. Now, however, it is enjoying unhappy fame: as the centre of an experiment in multiculturalism wrecked by intolerance. The story defies neat conclusions.

In September 2001 Karin Heremans became headmistress of the Atheneum, which has students of 45 nationalities. The September 11th attacks on America came ten days after she took charge, and her schoolyard became the scene of "very intense" arguments. Ms Heremans responded by working hard to turn her school into a place of "active pluralism". A project about Darwin was led by science teachers but backed by a dialogue among the school's religious instructors. A local composer wrote a work with Christian, Jewish and Muslim passages for pupils to sing. There were debates on sexuality and elections. A fashion show saw girls invited to wear Muslim headscarves, or not: one teenager wore half a scarf to symbolise indecision.

In France Muslim headscarves, along with all ostentatious religious symbols, have been banned at state schools since 2004. It helps that France has a record of separating religion from the state going back more than a century (even a Christmas nativity play would be unthinkable at a French state school).

By contrast Belgium has muddled through. Most schools in Flanders are state-funded but church-run (and pretty secular in outlook). All schools have been left to craft their own rules on headscarves and, in recent years, Antwerp's schools began banning religious clothing, leaving just three that allow scarves—among them the Atheneum. Ms Heremans soon noticed Muslim girls moving to her college. Between 2006 and 2008 the proportion of Muslim pupils at the Atheneum rose from half to 80%.

"At the beginning, I didn't see a problem," she explains. But then, a number of "very conservative" families moved their daughters to the school. By 2007 about 15 girls came to school wearing all-concealing robes and gloves, with only their faces showing. Ms Heremans confronted them. "I said: 'You're stigmatising yourselves. You're breaking with society by wearing those clothes.'" The girls replied that she

was stigmatising them. Pupils began donning longer scarves. Others started covering up at school, even though teachers saw the same girls walking in the streets unveiled. When questioned, such girls said they felt uncomfortable at school without head coverings. In 2007 it proved impossible to organise a two-day school trip to Paris—a longstanding annual treat for 15-year-old pupils. "Suddenly it was a problem for girls to stay overnight. Their older brothers had to come too," Ms Heremans says. Most of all, an oppressive, "heavy" atmosphere hung over the schoolyard.

On September 1st Ms Heremans reluctantly reversed herself and banned headscarves at her school. This triggered some nasty protests, including threats from a small clutch of hardliners. The results have been serious: about 100 of the school's 580 pupils have left. Local politicians have raised fears that some may not get an education at all. On September 11th the Flemish education board banned religious symbols in all 700 secular state schools under its control, including the Atheneum. (Religious schools remain free to set dress codes.) It was the opposite of what Ms Heremans once sought, she admits. "But now I feel supported." Some older girls quietly thanked her, saying: "You've no idea of the pressure we were under."

Yet it is not just fiery conservatives who have condemned Ms Heremans. "Boss of my own head", or BOEH in the Dutch acronym, is a feminist group with a mixed Muslim and non-Muslim membership. Its members protested outside the school with whimsy, turning up with sieves and toys on their heads. A spokesman for BOEH, Samira Azabar, says that schools are making it harder for Muslim girls to be "emancipated" through education. She is probably right. Other Antwerp schools banned scarves on the ground of equality but in reality, says Ms Azabar, they wanted to repel pupils from poor backgrounds who might pull them down academic league tables. Ms Azabar dislikes the idea of all-Muslim schools, thinking them bad for integration in the community. But barring scarves "doesn't help girls"; in her view, Ms Heremans has "given up the battle".

The paradox of liberalism

In short, the story of the Atheneum is complicated. Unintended consequences abound. There are people of goodwill on both sides, and actors with murkier motives. The row will probably lead to the establishment of Muslim state schools in Antwerp: the city already has Catholic and Jewish schools. Patrick Janssens, the city's mayor, regrets this, saying he is "not particularly in favour" of single-faith schools. He puts his trust in long-term development: as more Muslims go to university, or feel that society offers them equal opportunities, they will be "liberated" and "realise that religion is not dominant over all other values."

The story of the Antwerp Atheneum is the latest example of a paradox: how should liberal, tolerant Europeans protect their values, even as they protect the rights of less liberal minorities in their midst? Blanket laws banning headscarves are hardly a liberal solution. But Belgium's piecemeal approach left Karin Heremans running something approaching a ghetto-school. Distrust anyone with a simple answer.

Economist.com/blogs/charlemagne

Northern Ireland

Hanging in there

Sep 17th 2009 | BELFAST
From The Economist print edition

For all the frissons, peace and power-sharing are proving remarkably durable

Eyevine



POLITICIANS trooped back to the Assembly at Stormont this week, their mild partisan sabre-rattling little more than a ritual greeting after the summer break. In its two and a half years of existence, power-sharing has, against all expectations, provided a considerable degree of political harmony, even though gunmen and bombers have not entirely vanished from the scene.

Many predicted that this government of ancient foes, dominated by the loyalist Democratic Unionist Party and republican Sinn Fein, would produce a battle a day, yet the deal has so far proved surprisingly resilient. The funerals have practically stopped. Nearly all the guns and nearly all the paramilitary groups have gone. Most of the political action now takes place in the Assembly rather than on the streets.

Peace is overwhelmingly popular, for one thing, and the big republican and loyalist parties are working closely with each other, both determined to stay in power. But not everywhere is as harmonious as Stormont. The transformation in Northern Ireland is not yet a complete one, for there are still many problems to test the fledgling devolved government.

Terrorism, for example, has not disappeared. Though the IRA is effectively defunct and extreme Protestant groups have promised to junk their remaining weaponry within months, small but deadly splinters remain. Most notable are the republican micro-groups, which include some mainstream IRA veterans but are mostly composed of impressionable youths.

In January these dissidents attempted to attack an army base in County Down, abandoning a 300-pound bomb nearby. Two months later they caused a security and political crisis when they killed two soldiers in Antrim and a police officer in Armagh. In the past few weeks they tried to wipe out a police patrol with a 600-pound bomb near the south Armagh border, and planted devices at the homes of relatives of a police officer in Londonderry.

No one was injured in the most recent episodes, and Catholics and Protestants united to condemn those in March. But the 1998 Omagh bomb, when the so-called Real IRA killed 29 people, is in the communal memory as an example of what even a small and relatively disorganised gang can do. Sinn Fein rightly denounces the dissidents as "minuscule and unrepresentative", but the police are also correct in saying that the threat they pose is "severe".

The persistence of such small but potentially lethal groups creates big problems, not least for the newish Police Service of Northern Ireland. With the British army no longer on active service, the police are now in charge. The activities of these destructive remnants inevitably hinder progress towards the creation of a civilian force geared to community policing.



And terrorists with large explosive devices are not the only folk disturbing the peace, for at a less dramatic level there is much to suggest that this remains an unsettled society. Police statistics show that, in a region of around 1.8m people, over 1,500 sectarian incidents and attacks were logged in the year through March, with more than 60 emergency evacuations since then. Many parts of Northern Ireland are as tranquil as any in Britain, but in others stone-throwing, street attacks and even petrol-bombing of Protestant and Catholic homes and buildings are not infrequent. Much of this violent vandalism is generated by bitter controversies over loyalist marches, which continue to cause problems in out-of-the-way villages such as Rasharkin in County Antrim.

Such incidents rarely result in deaths, though in May Kevin McDaid, a Catholic father of four, perished after street clashes over the display of flags in the normally peaceful town of Coleraine, County Londonderry. And to these sectarian confrontations must be added a further 1,000 or so racist incidents of the type which in June caused scores of Romanians to flee from Belfast. Though rising immigration has provoked tensions elsewhere in Britain too, that episode demonstrated that the Troubles have left behind in Northern Ireland an inarticulate underclass that all too readily resorts to violence. In that instance it was young loyalists who were so balefully xenophobic. Undereducated and generally unemployed, they have seen no peace dividend and feel little identification with the political process or its participants.

The Stormont administration frequently condemns both sectarian and racist violence but has done little to combat the divisions that produce them. Instead it has concentrated on making devolution work and learning to run the public services.

In doing so it has been curiously sheltered from the effects of the downturn, even though the local economy is unhealthy. Unemployment has risen but, at 6.7% in the three months to July, it is still less than the British average (7.9%), largely because a bloated public sector pays the wages of more than a third of the workforce. House prices, which shot up in the mid-2000s, were 22.2% lower in July than a year earlier, on figures from the Department for Communities and Local Government—a far steeper fall than in England, Wales or Scotland. Many think prices have touched bottom, however, and Northern Ireland seems to have avoided the worst of the recession. Will its luck hold as Britain's public finances continue to deteriorate?

Some in Northern Ireland complacently assume that the province will remain a protected political species, safe in the expectation of generous central-government support. But senior politicians suspect this state of affairs will end next year. Whoever wins the general election due by June 3rd will surely look to reducing the flow of money from Whitehall to Belfast. The threat is not likely to disrupt power-sharing fundamentally; it may well unite all parties against a common enemy—the Treasury. Much of the partisan rowing these days—over the devolution of policing to Stormont, for example, which republicans want now and loyalists are less keen on—seems designed to make London think the settlement is more precarious, hence more in need of subsidy, than it is.

Though many issues remain unresolved, and the emotions from decades of conflict are still raw for many, power-sharing has so far proved flame-proof against all challenges. Belfast politics used to resemble trench warfare; in the new dispensation the main protagonists have ended up in the same trench.



Labour and the trade unions

My enemy's enemy

Sep 17th 2009
From The Economist print edition

A Tory government may make the unions less radical, not more

John Harris-reportdigital.co.uk



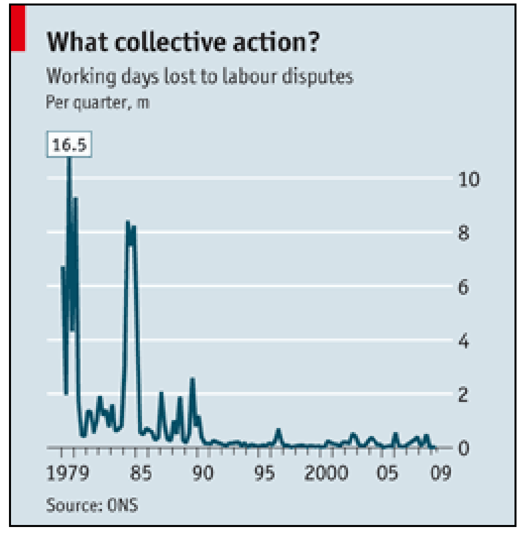
THE loudest one in the room, as on-screen mafia men like to say, is usually the weakest. This week's Trades Union Congress (TUC), an annual gathering of organised labour, was a cacophony of truculence. On September 14th delegates voted to back strikes to prevent public-sector job cuts. Brendan Barber, the TUC's leader, noted that spending cuts once caused "riots on the streets". And on the eve of the congress, Derek Simpson, joint general secretary of Unite, the largest private-sector union, described some on the right of the Labour Party as "thick" and even as "Tories".

But beneath the bluster, the unions face tough times. Unemployment has reached almost 2.5m, and will keep rising. A Conservative government is likely to emerge from the general election that must be held by June 3rd. And reductions in spending will be sought by whichever party wins. In his speech to the TUC on September 15th Gordon Brown, the prime minister, finally joined the Tories in using the word "cut". He insists that he will protect "front-line services", but the "inefficiencies" and "lower-priority budgets" he says he will target are likely to affect union members too. Meanwhile the Liberal Democrats, not long ago to the left of Labour on fiscal issues, have gone further than the two main parties in specifying what spending they would cut (see article).

Even weakened, the unions could make life hard for a Tory government, whose market-based reforms for schools will provoke no less union ire than its as-yet-vague spending plans. But their influence will be greater on Labour in opposition. The financial whip hand that union barons have over the party is of little use now for if they withhold donations, as bolshier elements wish, a Tory victory becomes more certain. But after the election, the party could be shaped by its paymasters. The unions are also using their muscle to install placemen as Labour parliamentary candidates. And, as the unions make up one-third of the party's electoral college, those who aspire to be the next Labour leader must court them assiduously.

All this may herald a leftward drift as dramatic as the last time Labour entered opposition in 1979. The unions have been itching for the old religion since the turn of the decade, when strike action began rising slightly (see chart) and left-wingers such as Mr Simpson, Mark Serwotka of the Public and Commercial Services Union (PCS) and Bob Crow of Rail, Maritime and Transport became general secretaries.

Yet the unions' improving relations with the Conservatives suggest a degree of political realism. Mr Barber has met David Cameron and may yet invite the Tory leader to speak at next year's TUC congress. For the first time in a decade, the PCS will hold a fringe event at the Tories' annual conference next month. Richard Balfe, a former Labour MEP who defected to the Tories in 2002, is Mr Cameron's envoy to the union world. And 18 years in the cold under the previous Tory government—and the decline in union membership that came with it—taught most unionists the futility of uncompromising militancy.



It may also have taught them the folly of favouring ideological purism over electability when choosing the next Labour leader. Mr Simpson has named Ed Miliband as his favoured candidate to replace Mr Brown. The energy secretary is slightly to the left of his brother, David, the foreign secretary, and well to the left of Blairites such as Lord Mandelson, the first secretary of state. But he has fewer socialist bona fides and union contacts than other possible candidates, such as Harriet Harman, the party's deputy leader, or the thoughtful backbencher Jon Cruddas. Pragmatism, not decibels, may end up being the unions' way of dealing with their weakness.

New ideas for welfare reform

Thanks, but no thanks

Sep 17th 2009
From The Economist print edition

Hard times make an expensive benefits shake-up a hard sell

IN THAT foreign land of Britain before the credit crisis, the Conservative opposition party started to fret about a "broken society". The new Tory mission, now that Thatcherite remedies carried forward by Blairite Labour had saved the economy, was to tackle the outlands of a prospering society—the bleak estates where too many people were marooned, out of work, luck and hope. If that ambition cost money in the short-term, a Conservative government could draw upon the "proceeds of growth"—tax revenues generated by a never-ending economic expansion.

Now it is Britain itself that is broke, and any plan for repairing social breakdown that comes with a bill attached is likely to get a dusty reception. That may well be the fate for some bold proposals for reforming welfare from the Centre for Social Justice, a right-leaning think-tank established by Iain Duncan Smith, a former Tory leader.

Its new report argues that a malfunctioning benefits system lies at the root of many social evils. For one thing, it helps to explain why no adult works in 16.9% of working-age households, a rate virtually unchanged from a decade ago despite Labour's attempts to move people off welfare and into employment. For another, it tends to undermine the family. According to the think-tank, 1.8m low-earning couples are worse off because they live together. That penalty encourages couples to split up, which is often bad for children. Add to this the bewildering complexity of an array of different benefits, and you get a welfare system that is not working.

The underlying problem is that workless households get caught in the benefits trap. If an adult takes a low-paying job, most of the earnings will be offset by the swift withdrawal of benefits and the imposition of income tax and national-insurance contributions. The "highly influential word of mouth message", says Mr Duncan Smith, is that "progression into work simply isn't worth the hassle".

The solution, says the think-tank, is to increase the reward for getting a job. Eight main benefits would be merged into just two, which would be withdrawn less swiftly and at a less onerous rate for claimants who find work. That should free many people from the benefits trap.

These proposals have their merits, not least their emphasis on tackling the barriers that keep so many in a workless limbo. But there are two snags. First, the welfare system may appear wilfully complicated, but that does not mean simplifying it will be simple. One reason is that the circumstances of claimants, ranging from lone parents to the newly unemployed to those on incapacity payments, vary greatly. Any government will tread carefully in clearing a path through this minefield. "Simplifying benefits looks easier from outside rather than inside government," says Mike Brewer of the Institute for Fiscal Studies.

Second, the proposal comes with a price tag. The reform would add £3.6 billion ($5.9 billion) to the benefits bill. The think-tank argues that the overhaul would eventually save money. But a Treasury drowning in red ink is likely to score the costs as actual and the savings as notional.

The Conservatives have responded cautiously to the report, saying merely that it raises "interesting questions". If the Tories do win the election, they will have an even more compelling question to answer, namely how to mend Britain's ravaged public finances. That may crowd out costly efforts to fix a "broken society".



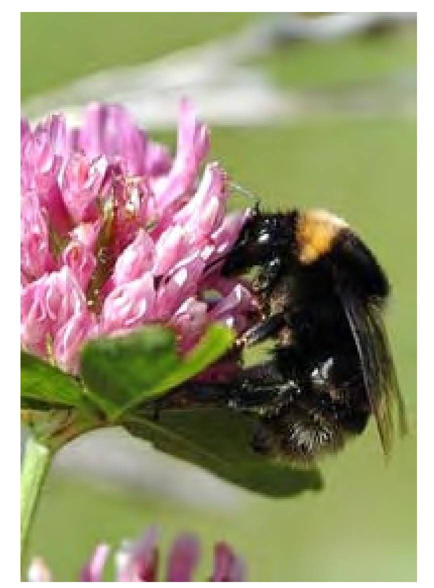
The short-haired bumblebee

Bzzzt, it's back

Sep 17th 2009
From The Economist print edition

A black-and-yellow-striped émigré returns home after a century

BBCT



Coming home

MORE than 100 years ago, labourers clearing ditches in Kent were paid a bounty for each bumblebee they found. New Zealanders wanted the long-tongued types to pollinate the red clover they used for sheep pasture, so that they would not have to import and re-sow the clover each year. In December 1884, 282 bumblebee queens left London for Wellington on the "Tongariro", one of the first steamships with a refrigeration unit, in which they could safely hibernate. Forty-eight survived the journey, and their offspring are flourishing on South Island today.

One of the deported species, the short-haired bumblebee, has died out in Britain. But descendants of its émigré cousins may soon be making the long trek home. Reintroduction has been mooted before, but bees are prone to lethal jet-lag and long-tongued bumblebees are hard to breed in captivity. Now the Bumblebee Conservation Trust thinks it has worked out how to do it.

The key, according to recent work by Jaromir Cizek, a Czech bumblebee enthusiast, is to feed the queens a high-quality mix of nectar and pollen freshly collected by bumblebees, not the low-grade stuff tolerated by their close relatives, the domesticated honeybee. That, his experiments suggest, will persuade the fussy eaters to lay eggs. A new generation can then be kept in sterile conditions, to minimise the chance that nasty foreign diseases are brought back to Britain on the return journey. If the plan works, the second generation of queens will be fertilised, chilled to induce hibernation and stored inside old-fashioned hair rollers sealed at both ends with corks. Thus protected, they will be flown to Britain and released in Dungeness, Kent, near where the species was last spotted in 2000. Farmers have been planting masses of red clover to welcome them.

The return of the short-haired bumblebee would be a small piece of good news amid much bee-related gloom. Honeybees are under threat from new and strange diseases; meanwhile intensive farming means that there are fewer of the wildflowers bumblebees sip nectar from, and fewer hedgerows in which they can build their nests. Two species have died out, and of the 24 remaining ones seven are threatened and only six are thriving. That is a problem for agriculture: some commercial crops, such as apples, tomatoes and strawberries, need bumblebees to pollinate them.

As novel species out-compete native ones (American grey squirrels in Europe; European and Asian knapweed in America), globalisation often threatens biodiversity. But "abroad", it seems, is a good place to back up cherished locals too.

Risk, regulation and children

A toxic mix

Sep 17th 2009
From The Economist print edition

A petting farm closes; a database opens

Illustration by David Simonds



THE chance to feed and stroke animals is a big part of the charm at petting farms. This summer, though, the hands-on approach has led to grief at Godstone Farm and Playbarn in Surrey. Some of its animals, it turns out, have been carrying the virulent 0157 strain of *Escherichia. coli*, a bacterium that in its benign forms colonises most people's guts. Forty cases have now been confirmed in what is likely to be Britain's largest-ever outbreak of *E.coli* poisoning spread by animals (contaminated food is a more common source). Fourteen children are in hospital, and four of them are seriously ill.

E. coli poisoning is a known risk of petting farms. Infected animals show no symptoms, and infected humans can take 12 days to become sick, so many people may be exposed before health officials act. The past two decades have seen a series of similar outbreaks in America, and Canadian officials are investigating one at an agricultural fair in Vancouver.

Particularly exercising public opinion, though, is the lackadaisical response of the Health Protection Agency, the government body charged with guarding the public against infectious diseases. It first realised that there might be a problem at the farm on August 27th, and merely advised isolating high-risk animals (cows, sheep and goats) and posting more notices about the importance of washing hands. Not until September 12th, after cases that could not have been caused by infection before those precautions were taken, did it order the farm to close. Worse still, on September 16th it admitted it had been notified of cases on August 20th and 25th, but had failed to connect them with the farm.

In weird parallel, another quango set up to safeguard the public is also in the headlines—but this time the story is about overkill, not complacency. The Independent Safeguarding Authority, which will open for business on October 12th, was set up after the murders of two ten-year-olds, Holly Wells and Jessica Chapman, in 2002. Despite previous accusations of rape and having sex with children, the culprit, Ian Huntley, had found a job as a school caretaker. A subsequent inquiry called for a new agency to vet all those working with children and other "vulnerable" people.

Campaigners for privacy and civil liberties have been sounding the alarm for ages over the new agency's tentacular remit. But only now has it entered the public consciousness. A quarter of all adults will be on its database: not only those employed by hospitals or schools, but everyone who works with children, the sick and the elderly "frequently" or "intensively". Those organising children's sports, or running social activities at day-care centres for old people, for example, are likely to come within its scope. Though some charities are keen on it, others rue the likely decline in volunteering. Children's authors as eminent as Anne Fine, Michael Morpurgo and Philip Pullman say that they will stop visiting schools rather than apply for clearance.

The uproar has had some effect: Ed Balls, the secretary for children, said on September 14th that there would be a review of just what "frequent or intensive" should mean. (At the moment, three times in one month, or once a month for three months—among other combinations—count.) But few critics are mollified. "The worst of all worlds—intrusive, ineffective and enormously expensive", say the opposition Tories, who would scrap the scheme, along with the national identity register and children's database being developed. Chris Stevenson, the detective who led the investigation into the disappearance of Holly and Jessica, points out that the girls crossed Mr Huntley's path not because of his job (he worked at a different school), but because they knew his girlfriend, who had worked at their school. It is hard to see

that the new agency would have made any difference at all.

Executive pay

Maligned, or misaligned?

Sep 17th 2009
From The Economist print edition

The way company bosses are rewarded is in the spotlight

SHAREHOLDER revolts, like the one in May over the fat pay packets of Royal Dutch/Shell's bosses, are rare. More than half of the investors at the company's annual general meeting, led by Standard Life, an insurer, voted against what they saw as the flouting of agreed performance measures in setting top executives' pay. A normally routine measure on remuneration backfired badly, among accusations of greed and underhandedness.

For Shell it was appalling publicity. But there has been little visible impact so far on its pay policy, except that Sir Peter Job is stepping down as chairman of the group's remuneration committee on October 1st (he will remain a member). Shell says it is still consulting its big shareholders.

Investors frequently reap nothing but frustration when they seek to restrain the financial aspirations of corporate bosses. Many don't even try. For all the public outcry over soaring bank bonuses, for example, the British government, the controlling shareholder in the rescued banks RBS and Lloyds, has not dared to rock the boat by curtailing them explicitly. The latest revelations about the so-called Phoenix Four, the consortium that bought MG Rover Group in 2000 for £10, have stoked public outrage over the perceived greed of some bosses still further. According to a government report published on September 11th, by the time Rover filed for bankruptcy in 2005 the four had paid themselves around £36m in salaries and special dividends, all sanctioned by auditors and lawyers. Around 6,000 workers lost their jobs.

Executive pay in Britain, as in America, has risen sharply. The average pay package of the chief executive of a FTSE-100 company, including his pension and long-term incentive plan, increased from £1m in 1998 to close to £4m in 2008, on figures from MM&K, a remuneration consultancy (see chart 1). In 1998 the average FTSE boss made 47 times as much as a typical employee; in 2008 he earned 128 times as much. British firms pay a little less than the Irish and a bit more than the Germans, according to Watson Wyatt, another consultancy. And long-term incentives tend to be a bigger part of the British package (see chart 2).

The sky's the limit 1

Average remuneration of FTSE 100 CEOs, £m

Salary | Other benefits | Pension | Bonus | Options | Long-term incentives*

1998, 2000, 02, 04, 06, 08 — 0, 1, 2, 3, 4

Source: MM&K — *Expected value of award

One reason for rapidly rising executive pay is globalisation. Top bosses offer themselves for hire from Sydney to Frankfurt, and a salary offered in one big city sets a floor in another. A second is the incentives offered by private-equity funds to keep executives at firms when they take them over, or to motivate new ones. Stratospheric but heavily dependent on financial performance, these have raised the rates others must pay, often with no clawback if things go wrong. Another pressure driving up pay may be the growing "industry" of remuneration consultants, who sometimes charge fees dependent on the size of the package that emerges. And disclosure of eye-popping deals stokes competition for higher rewards.

Paying top executives a conspicuous bundle might be justified if it meant that a firm was much better managed, but the connection is often weak. And at a time when taxpayers are underwriting bank profits, lavish pay deals in that sector strike many as just plain offensive. Various bodies are seeking ways to align pay more closely with companies' longer-term fortunes. In Britain, the Financial Services Authority, which worries that some bonus deals encourage reckless risk-taking, says it may force banks that dish them out to hold more capital. Two government-sponsored

reviews—one by Sir David Walker, a former central banker, and another by the Financial Reporting Council, an accounting-standards body—are likely to demand that shareholders police pay more effectively. Tell that to Shell's investors.



Trouble at the National Archives

Pricing the past

Sep 17th 2009
From The Economist print edition

A row over budget cuts is pitting academics against amateurs

National Archives



Coming soon to a computer screen near you

IN A grey concrete fortress, glowering at an otherwise leafy Kew over a moat-like pond, the National Archives guards Britain's official records, reflecting almost 1,000 years of history. In one reading room academics and students pore silently over crumbling old documents; in another chatty amateur researchers from all over the world study census and family records in search of local history and their long-lost ancestors.

This summer, however, the archive's bosses succeeded in upsetting all their user groups. They want to lower running costs by 10%, anticipating a squeeze in public funding. Their proposals include cutting opening hours by 16% and reducing staff and access to documents, some of which will be stored in a Cheshire salt mine. The expensive process of digitising the archive's treasures will continue, but only for documents that lots of people are likely to pay to see. Folk are being nudged away from viewing original material at the archive, free of charge and advised by specialists, toward its pay-per-view website.

Many fellows of the Royal Historical Society, Britain's largest grouping of academic historians and researchers, fret that their interests are being disregarded. Academic advisory groups at the archive have withered away in recent years and, to cap it all, consultation on the proposed cuts closed on September 12th, just as many researchers were returning from working holidays abroad. But it isn't only academics spluttering over their tea; some local and family history buffs are unhappy with the cuts too, particularly the reduced hours during which expert assistance will be available at Kew.

Britain's archivists have traditionally provided an exceptional public service, especially compared with their counterparts abroad. At America's national archive, for example, which has a budget more than four times its British cousin's, fewer documents are fetched for readers.

They are right, too, to take the budgetary initiative in these straitened times. But the perennial tough choice between supporting often rarefied research and attracting the masses has got tougher, and solutions are proving elusive. The archive has hoped that putting more material online would cut the numbers trekking to Kew. In vain, it seems: document downloads were up by nearly 13% this August from the same month a year earlier, yet at least as many visitors showed up in person. The archive is, in a sense, the victim of its own success.

Other scholarly institutions face similar choices these days. At the Darwin Centre in London's Natural History Museum, which opened on September 15th, this gulf has been uneasily bridged. Visitors can watch researchers at work behind glass and even ask questions over an intercom, treating them rather like the specimens they are working on.

Bagehot

The last laugh

Sep 17th 2009
From The Economist print edition

Why the Liberal Democrats may yet triumph against the global conspiracy to marginalise them

Illustration by Steve O'Brien



AMID the inevitable jokes about sandals and granola, there is likely to be one persistent, carping refrain at the Liberal Democrats' conference in Bournemouth next week. Why—when the government is in terminal decline and the Conservative opposition less than a knockout—aren't the party and its likeable leader, Nick Clegg, capitalising on it? If not now, why bother?

This is a lazy question, and the wrong one. The real mystery about the Lib Dems is not why they aren't performing better, but why they aren't doing much worse.

Consider the Himalayan obstacles they face. It is only a slight exaggeration to say that, most of the time, almost nobody listens to a word they say. As one of Mr Clegg's predecessors put it, where the prime minister wakes up thinking about what he has to do, and the Tory leader ponders what to say, the Lib Dem chieftain wonders how to make anybody pay him the slightest attention. The proliferation of news outlets might, in theory, have helped the Lib Dems increase their exposure. It hasn't: round-the-clock news channels and blogs have been as captured and captivated by the car-crash spectacle of Gordon Brown's demise and by David Cameron's rise as have the traditional media.

This attention deficit, of course, derives from the inherently duopolistic nature of British politics. As they never tire of repeating, the Lib Dems secured almost a quarter of the vote at the last general election but, under the distorting first-past-the-post system, won less than a tenth of Westminster seats. The structure of politics both reflects and reinforces a binary view of its possibilities: many Anglo-Saxon minds seem to find it hard to grasp a political choice involving more than two options. True, in the past few years the British electorate has fractured, with more voters turning away from Labour and the Tories, a trend sometimes cited as an encouragement by Mr Clegg. But his party has not been the main beneficiary of it. Smaller ones—the Greens, the Scottish Nationalists and so on—have sucked up many of the protest votes that the Lib Dems might once have hoped to garner.

Such is the historical lot of the third party. But Mr Clegg faces an extra problem. His party has achieved incremental success at the last three elections (it now has 63 MPs), largely because the Conservatives, the Lib Dems' main opponents in marginal southern constituencies, were floundering. In Mr Cameron the Tories have a disturbingly presentable front man, able to woo the southern types whom his harsher, balder predecessors alienated. The Tories also enjoy funds that dwarf the Liberal Democrats' (and Mr Clegg does not habitually gad about in private planes).

With their conference approaching, some Lib Dems have muttered sardonically that there is a global conspiracy to do them down. Last year's jamboree was overshadowed by the demise of capitalism; this year's faces competition from the G20 meeting in Pittsburgh. That might be a tad paranoid. But the tide of politics, as well as the rules, does indeed seem to be against them.

Preparing for government

Given all that, the party's showing in opinion polls—they are bobbing along at between 17% and 21%—and recent results in local contests look respectable. The complaint that Mr Clegg ought by now to have led his followers to the sunny polling uplands of the mid-20s is over-harsh. So too, Bagehot submits, is its gloomy prophetic corollary—the widespread notion that, having failed to make a mid-term breakthrough, the Lib Dems are destined to be brutally culled at the forthcoming election. That is partly because, in a campaign, the policies that they have spent their obscurity developing will get the hearing some of them deserve.

The one subject on which the party, and especially Vince Cable, its shadow chancellor, have sometimes been able to assert themselves is the economy—deservedly, since their position has often been more grown-up than Labour's or the Tories'. They accepted the government's case for a fiscal stimulus (which the Tories dogmatically opposed), while doubting the specific form it took (a VAT cut). Eschewing hysterical talk about national bankruptcy, Mr Cable has been more detailed than his counterparts about how the government's spending and deficit might be trimmed. In a fine pamphlet published on September 15th, he specified assorted defence projects that might be cut, and was frank about the need to reform public-sector pay and pensions.

But the Lib Dems may impress on other issues too. Mr Clegg is the only senior politician to voice the legitimate doubts about Afghanistan that others routinely air in private—a service that even supporters of the war ought to welcome. The Lib Dems emerged relatively unsullied from the parliamentary-expenses debacle; they may even have a point when they link the moral laxity of some MPs with a voting system that entrenches too many of them in safe seats. They have better and more radical policies than the other parties for devolving power to local councils.

Mr Clegg's overall argument is that Labour's ingrained statism has failed. He is right. He goes on to contend that, just as Labour ousted the divided Liberals after the first world war, the Lib Dems are now intellectually equipped to oust it back, and to emerge as the Conservatives' main rival. That is perhaps overblown. But a humbler optimism may be justified. A sound election platform, plus a powerful national urge to throw Labour out, may allow the Lib Dems to hang on to most of the southern seats that look vulnerable to the Tories, while taking a few from Labour elsewhere. Even if the outcome is not the Lib Dem nirvana of a hung parliament, with its mythical potential for coalitions and pacts, the party may emerge stronger than the carpers predict.

The Lib Dems' job for most of the time between elections is simply to stay in the game. They have—and it is just possible that Mr Clegg and his granola-eaters will have the last laugh.

Economist.com/blogs/bagehot



WORLD
INTERNATIONAL

Developing countries and global warming

A bad climate for development

Sep 17th 2009
From The Economist print edition

Poor countries' economic development will contribute to climate change. But they are already its greatest victims

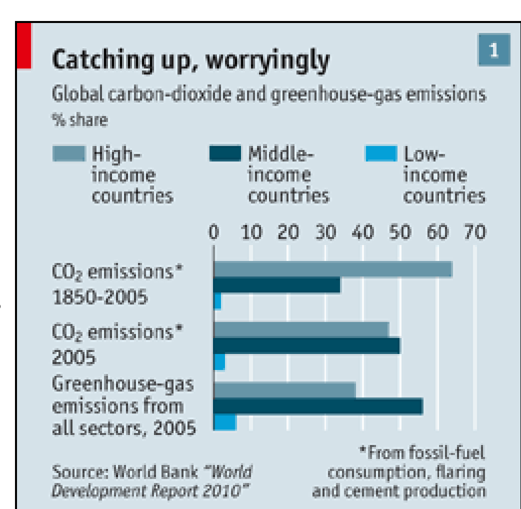
AP



IN LATE April Mostafa Rokonuzzaman, a farmer in south-western Bangladesh, gave an impassioned speech at a public meeting in his village, complaining that climate change, freakish hot spells and failed rains were ruining his vegetables. He didn't know the half of it. A month later Mr Rokonuzzaman was chest-deep in a flood that had swept away his house, farm and even the village where the meeting took place. Cyclone Aila (its effects pictured above) which caused the storm surge that breached the village's flood barriers, was itself a plausible example of how climate change is wreaking devastation in poor countries.

Most people in the West know that the poor world contributes to climate change, though the scale of its contribution still comes as a surprise. Poor and middle-income countries already account for just over half of total carbon emissions (see chart 1); Brazil produces more CO2 per head than Germany. The lifetime emissions from these countries' planned power stations would match the world's entire industrial pollution since 1850.

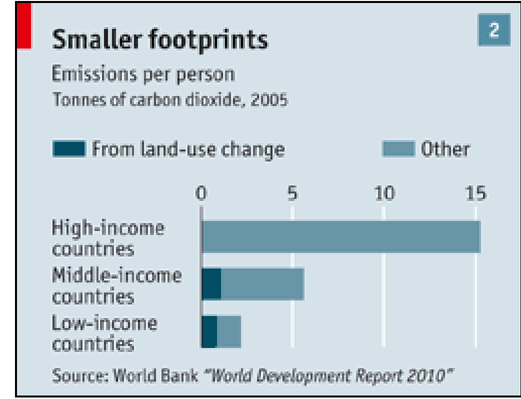
Less often realised, though, is that global warming does far more damage to poor countries than they do to the climate. In a report in 2006 Nicholas (now Lord) Stern calculated that a 2°C rise in global temperature cost about 1% of world GDP. But the World Bank, in its new World Development Report*, now says the cost to Africa will be more like 4% of GDP and to India, 5%. Even if environmental costs were distributed equally to every person on earth, developing countries would still bear 80% of the burden (because they account for 80% of world population). As it is, they bear an even greater share, though their citizens' carbon footprints are much smaller (see chart 2).



As December's Copenhagen summit on climate change draws near, poor countries are expressing alarm at the slow pace of negotiations to replace the Kyoto protocol. Agreed (partially) in 1997, this bound rich countries to cut their greenhouse-gas emissions by 5.2% from 1990 levels by 2012.

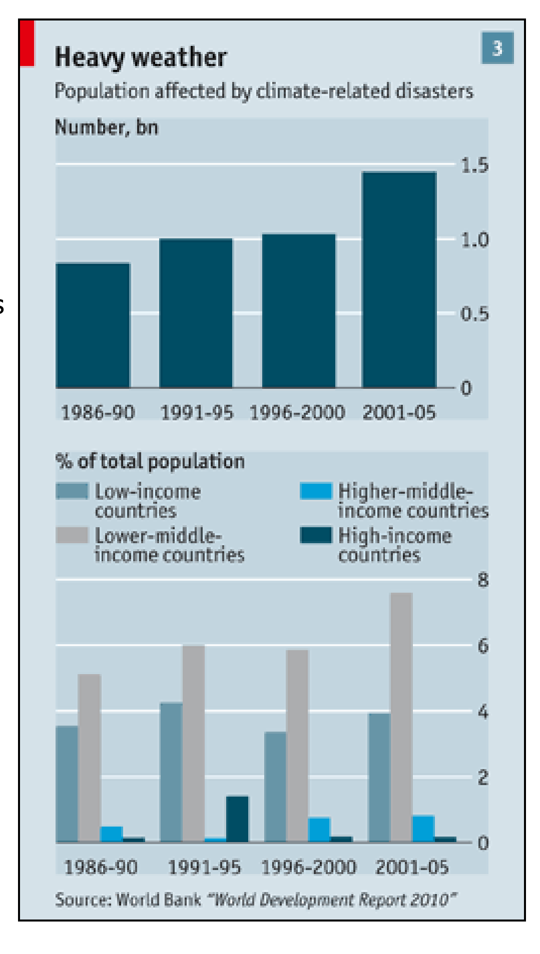
Counting the cost of global warming is hard because no one really knows how much to attribute to climate change and how much to

other factors. But one indication of its rising costs is the number of people around the world affected by natural disasters. In 1981-85, fewer than 500m people required international disaster-assistance; in 2001-05, the number reached 1.5 billion. This includes 4% of the population of the poorest countries and over 7% in lower-middle-income countries (see chart 3).



In all, reckons the World Health Organisation, climate change caused a loss of 5.5m disability-adjusted life years (a measure of harm to human health) in 2000, most of it in Africa and Asia. Estimates by the Global Humanitarian Forum, a Swiss think-tank, and in a study in *Comparative Quantification of Health Risks*, a scientific journal, put the number of additional deaths attributable to climate change every year at 150,000. The indirect harm, through its impact on water supplies, crop yields and disease is hugely greater.

The poor are more vulnerable than the rich for several reasons. Flimsy housing, poor health and inadequate health care mean that natural disasters of all kinds hurt them more. When Hurricane Mitch swept through Honduras in 1998, for example, poor households lost 15-20% of their assets but the rich lost only 3%.



Global warming aggravates that. It also increases the chances of catching the life-threatening diseases that are more prevalent in poorer countries. In many places cities have been built just above a so-called "malaria line", above which malaria-bearing mosquitoes cannot survive (Nairobi is one example). Warmer weather allows the bugs to move into previously unaffected altitudes, spreading a disease that is already the biggest killer in Africa. By 2030 climate change may expose 90m more people to malaria in Africa alone. Similarly, meningitis outbreaks in Africa are strongly correlated with drought. Both are likely to increase. Diarrhoea is forecast to rise 5% by 2020 in poor countries because of climate change. Dengue fever has been expanding its range: its incidence doubled in parts of the Americas between 1995-97 and 2005-07. On one estimate, 60% of the world's population will be exposed to the disease by 2070.

Next, as Mr Rokonuzzaman's story showed, poor countries are particularly prone to flooding. Ten of the developing world's 15 largest cities are in low-lying coastal areas vulnerable to rising sea levels or coastal surges. They include Shanghai, Mumbai and Cairo. In South and East Asia the floodplains of great rivers have always been home to vast numbers of people and much economic activity. Climate change is overwhelming the social and other arrangements that in the past allowed countries and people to cope with floods. National budgets can ill afford the cost of improving defences. The Netherlands is also affected and is spending $100 per person a year on flood defences. In Bangladesh that sum is a quarter of the average person's annual income.

The biggest vulnerability is that the weather gravely affects developing countries' main economic activities—such as farming and tourism. Global warming dries out farmland. Since two-thirds of Africa is desert or arid, the continent is heavily exposed. One study predicts that by 2080 as much as a fifth of Africa's farmland will be severely stressed. And that is only one part of the problem.

Global warming also seems to be speeding up the earth's hydrologic cycle, causing both floods and droughts (more rains fall in shorter periods, with longer gaps between). In addition, by melting glaciers, global warming reduces nature's storage capacity. Two-thirds of the world's fresh water is stored in glaciers. Their melting leaves poor countries with less of a buffer to protect farmers against changing weather and rainfall patterns.

This kind of increasing unpredictability would be dire news at the best of times: hit by drought and flood, the land becomes less productive. It is compounded by another problem. The higher-yielding, pest-resistant seed varieties invented in the 1960s were designed to thrive in stable climes. Old-fashioned

seeds are actually better at dealing with variable weather—but are now less widely used. Reinstituting their use will mean less food.

In India the gains from the Green Revolution are already shrinking because of local pollution, global warming and waning resistance to pests and disease. A study for the Massachusetts Institute of Technology forecast that yields of the main Indian crops would decline by a further 4.5-9% over the next 30 years because of climate change. A recent assessment based on a large number of studies of what might happen in the long run if carbon continues to be pumped into the atmosphere found that world farm production could fall by 16% by the 2080s, and possibly by as much as 21% in developing countries. Although the timescale makes such figures no more than educated guesses, there is not much doubt that climate change is undermining the gains from intensive farming in developing countries—at the very time when population growth and greater wealth mean the world will need to double food production over the next three or four decades. By 2050 the world will have to feed 2 billion to 3 billion more people and cope with the changing (water-hungry) diets of a richer population. Even without climate change, farm productivity would have to rise by 1% a year, which is a lot. With climate change, the rise will have to be 1.8%, says the bank.

If these myriad problems have a silver lining, it is that they give developing countries as big an interest in mitigating the impact of climate change as rich ones. As the World Bank says, climate-change policy is no longer a simple choice between growth and ecological well-being.

Sideways to Copenhagen

In principle that shift should make a climate-change deal in Copenhagen more likely, by increasing the number of countries that want an agreement. But two big problems remain. First, the poor countries want large amounts of money. To keep global warming down to an increase of 2°C, the World Bank calculates, would cost $140 billion to $675 billion a year in developing countries—dwarfing the $8 billion a year now flowing to them for climate-change mitigation. The $75 billion cost of adapting to global warming (as opposed to trying to stop it) similarly overwhelms the $1 billion a year available to them.

Second, poor countries see a climate-change deal in fundamentally different terms. For rich countries the problem is environmental: greenhouse gases are accumulating in the atmosphere and must be cut, preferably using the sort of binding targets recommended by the Intergovernmental Panel on Climate Change. For developing countries the problem is one of fairness and history: rich countries are responsible for two-thirds of the carbon put into the atmosphere since 1850; to cut emissions in absolute terms now would perpetuate an unjust pattern. Poor countries therefore think emissions per head, not absolute emissions, should be the standard.

Moreover, targets set at national level have little effect in poor countries where public administration works badly. So rich and poor also disagree about the conditions attached to any money for mitigating or adapting to climate change. The rich see this as a sort of aid, designed for specific projects with measurable targets, requiring strict conditions. Poorer countries see the cash as no-strings compensation for a problem that is not of their making.

The cost of climate change gives developing countries a big interest in a deal at Copenhagen. But what sort of deal they want—and how hard they push for it—is another matter altogether.

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* "World Development Report 2010: Development and Climate Change". World Bank.

The car industry

Small isn't beautiful

Sep 17th 2009 | FRANKFURT
From The Economist print edition

Carmakers have escaped calamity. Now they face a big, long-term problem: people are moving to smaller vehicles

AFP



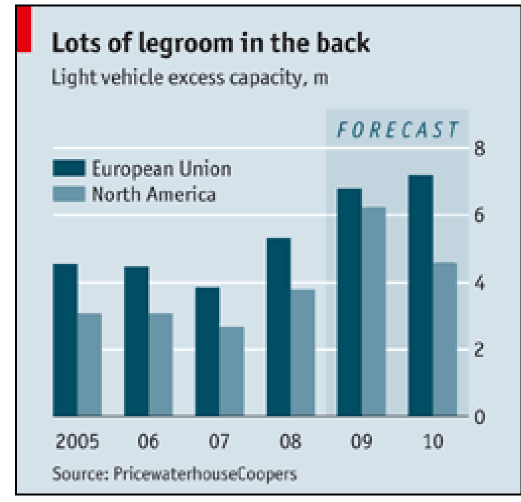
BIG motor shows are good barometers of the car industry's mood. Twelve months ago in Paris, in the wake of the collapse of Lehman Brothers, the mood was dread—the knowledge that something terrible was about to happen. At the beginning of this year, at the show in devastated Detroit, and a few months later in Geneva as Chrysler and General Motors prepared for bankruptcy, it was all about the struggle to survive. This week in Frankfurt the industry gave a sigh of relief, confident that the worst was over but painfully aware there would be no return to business as usual any time soon, if ever.

The sense of relief is understandable. After the collapse in sales and savage production cutbacks that took place in nearly every big market nine months ago—with the huge exception of China—volumes have started to rise as inventories are cautiously rebuilt. Balance-sheets appear to have been stabilised if not repaired. There is even a good chance that in the final quarter of this year some of the big carmakers will return to (very modest) profit, while others will do so next year. Credit, the lifeblood of the industry, is flowing again, albeit somewhat anaemically. Particularly in Europe, government-sponsored scrappage schemes have brought buyers back into the market. And manufacturers are now enjoying reduced costs, partly from lower raw-material prices and partly because they have laid off workers.

What has not happened is any substantial reduction in capacity, particularly in Europe where factories are capable of churning out 4m more cars than the market can take even in a good year like 2007 (see chart). Not long ago it was widely assumed that the downturn would be sharp enough to take out more than one big carmaker. For better or worse, governments have done their utmost to stop that happening. Like the bailed-out banks, GM was probably always too big to be allowed to fail. But few expected sickly Chrysler to survive in anything like its present form. The removal of Opel/Vauxhall, one of the weakest big producers in Europe, would have done the industry a power of good.

Yet, thanks to President Obama's auto task-force and a shotgun marriage with Fiat, Chrysler motors wearily on. German government largesse paved the way for Magna, an auto-parts firm, and Russia's Sberbank to buy a majority stake in Opel/Vauxhall from GM on the condition that no plants will be closed in Germany. GM even found buyers for tiny Saab in Koenigsegg, a boutique Swedish sports-car firm, and China's Beijing Automotive. Volvo, which is bigger and healthier than its Swedish rival, may be sold to Geely, China's biggest privately owned carmaker. Far from

consolidating, the European industry has instead gone in the opposite direction.



Although cuts at GM and Chrysler have removed some (though not enough) excess capacity in America, not a single car factory in Europe has closed so far. That is one reason why the carmakers assembled in Frankfurt believe that the normal strong, cyclical rebound may not happen this time. There are plenty of others.

One worry is the effect of withdrawing scrappage incentives. These have propped up demand this year, especially in Germany where they drove volumes to record levels. Optimists say that at least 70% of the scrappage purchases were incremental sales made to people who would not normally have bought a new car. But car-company bosses fear that volumes in Europe could slide next year unless "normal" new car buyers—well-off people and companies—return to the market. Even if scrappage schemes are continued or tapered, there may not be many buyers left who meet the qualifications.

Although the scrappage schemes have kept factories going, most of the action has been geared towards cheap, small vehicles which are less profitable for carmakers. They have thus weakened the "mix"—the balance of small and large vehicles sold—and reduced margins. The balance may swing back slightly next year, but the mix is threatened on a number of fronts in the longer term, raising doubts as to whether margins will return to their previous levels over the next few years.

To understand the importance of the mix, says Max Warburton of Bernstein Research, compare the cost of producing a small car such as the popular Fiat 500 with that of making a hulking sport-utility vehicle such as the Audi Q7. Mr Warburton calculates that the fixed costs are nearly identical, whereas the variable costs of making the Q7 (labour, raw materials and so on) are only about €10,000 ($14,700) higher for the Audi. Yet the Fiat sells for as little as €10,000, compared with a sticker price of at least €40,000 for the Audi. So a permanent shift toward smaller cars would devastate industry profits.

One big reason to expect such a shift is that the very cheap lease finance that manufacturers have relied on to stoke demand for their more costly cars, especially in America, Germany and Britain, is probably a thing of the past. Credit is unlikely to be so easily available again. Also, one of the ways leasing made more expensive cars seem affordable was by attributing to them high second-hand values after the lease was over. But higher volumes have dimmed the aura of exclusivity on which high residual values depend. BMW in particular has been badly hit by losses on returned cars and has cut the number of lease contracts it writes by a third.

A second threat to the mix, especially for the German premium makers, is demographic change. Arndt Ellinghorst of Credit Suisse says that by 2020 40% of new car buyers in developed markets will be over 60, compared with less than 30% today. Although the affluent old like premium brands, particularly Mercedes, they tend to want smaller, cheaper cars. Being mostly retired, they are generally buying a car with their own, rather than with a company's, money. Empty-nesters do not need much carrying capacity. Over-65s also drive 45% fewer miles than the average, which means their cars last longer. Together with the growing durability of modern cars, Mr Ellinghorst reckons that underlying sales in developed markets could fall by as much as 30%. For growth in the sales of big, powerful prestige cars, manufacturers will have to rely on emerging markets.

A third threat to the mix is the ratcheting up of emissions legislation in almost every important car market as governments struggle to meet ambitious carbon-reduction targets. That seems certain to reverse the trend in recent years toward ever heavier and more bloated vehicles. It is also forcing manufacturers to invest abnormal amounts to develop clean technologies in the hope that their bigger vehicles can be made socially acceptable and escape penal taxation.

The executives gathered in Frankfurt this week were aware that threats to the mix, and therefore profits, are long-term and structural rather than short-term and cyclical. They also acknowledge that the industry will have to wean itself from the habit of using profits from bigger cars to subsidise smaller ones, and find a way to start building downsized vehicles that make money. Nick Reilly, who heads GM's international operations, says that part of the answer is to adopt low-cost manufacturing techniques and not to load cheap cars with unnecessary technology. By contrast, Lewis Booth, Ford's chief financial officer, reckons that the solution is to make small cars that are as good to drive as bigger ones and charge accordingly. Half of the Fiestas sold by Ford in Europe come with the top-of-the-range Titanium specification and are

decently profitable, he says.

The problem confronts everyone (with the possible exception of Fiat, which has problems of its own), but it is most acute for the German premium makers, which dominated the Frankfurt show with their huge displays. Mercedes and BMW have enjoyed the best margins in the business, but they have lost lots of money on their small cars. BMW struggled to make a profit until recently even on its very successful Mini. Their rival Audi, being part of the massive Volkswagen Group, already has access to the technology and platforms it needs to make profitable small cars. To compete, Mercedes and BMW may have to do the unthinkable and join forces—either that, or risk their brands by forming partnerships with high-volume producers.

At the same time, the industry must tackle the problem of overcapacity in mature markets. Paradoxically, that may be easier once economies have emerged from recession and unemployment is no longer quite so high on the political agenda. More than anything, overcapacity undermines pricing power. The industry may feel it has come through a near-death experience in better shape than it could have hoped at the beginning of the year. But a return to health will take a lot longer.

Google's corporate culture

Creative tension

Sep 17th 2009 | MOUNTAIN VIEW
From The Economist print edition

The internet giant seeks new ways to foster innovation

Illustration by Claudio Munoz



FEW companies are as creative as Google, which serves up innovations almost as fast as its popular search-engine serves up results. This week the firm unveiled a new version of its Chrome web browser and launched Fast Flip, which lets users scroll through the contents of an online newspaper in much the same way that they leaf through its pages in print. On September 30th the company will roll out another fledgling product, Google Wave, for a test involving some 100,000 people. Billed as a revolutionary way to collaborate online, Wave is also the product of a new, more structured approach to innovation within the company.

For years Google has had a fairly informal product-development system. Ideas percolated upwards from Googlers without any formal process for senior managers to review them. Teams working on innovative stuff were generally kept small. Such a system worked fairly well while Google was in its infancy. But now that it is a giant with 20,000 employees, the firm risks stifling potential money-spinners with a burgeoning bureaucracy.

To stop that happening, Google has begun to hold regular meetings at which employees are encouraged to present new ideas to Eric Schmidt, the firm's chief executive, and Larry Page and Sergey Brin, its co-founders. It has also given some projects more resources and independence than in the past. Both moves are designed to ward off the conservatism that can set in as companies mature. "We are actively trying to prevent middle-agedom," explains Mr Schmidt.

Google Wave has benefited from this anti-ageing treatment. The new software allows people to create shared content that is hosted on Google's servers online, or "in the cloud". When they open Google Wave, users see three columns on their screens. The left-hand one contains folders and address books, while the middle column is a list of "waves"—online conversations users have initiated or signed up to. Clicking on a wave displays its contents in the right-hand column. People can post text, photos, web feeds and other things into a wave and exchange comments with one another instantly.

The software excites tech folk, some of whom reckon it poses a threat to Microsoft's SharePoint collaboration package. Inside Google the project has generated much enthusiasm too, plus some controversy. The Wave team deliberately distanced itself from Google's headquarters, choosing to be based in the company's Sydney office. And it insisted that its work be kept secret for a long time so its nascent idea was not subject to nit-picking criticism. Some Googlers felt this was a betrayal of the firm's open culture. "Not everyone inside the company thought that this was super cool," admits Lars Rasmussen, one of the two brothers leading the project, which was allowed to recruit dozens of software engineers to its ranks.

That has not dented Google's enthusiasm for creating more such teams. Mr Schmidt wants the number to grow from a dozen or so today to perhaps 50. The challenge, he says, is to find leaders with the calibre of Mr Rasmussen, who previously worked on an initiative that evolved into the successful Google Maps.

Some Google-watchers see a much bigger challenge. “Google has been masterful at coming up with a lot of ideas, but none of them has matured to become something that moves the revenue needle,” says Gene Munster of Piper Jaffray, an investment bank. In fairness to the company, that is partly because many of its popular innovations, such as Gmail, have been given away to boost search-related advertising, which accounts for almost all of Google’s revenues. But search has been suffering in the downturn: in the second quarter of 2009 Google’s revenues were $5.5 billion, barely 3% higher than the same period in 2008. Time, then, for the company to find new ideas that can make a big splash.

Comedy in America

Cheap and cheerful

Sep 17th 2009
From The Economist print edition

American television comedy was supposed to be dead. Ha ha

Kobal Collection



Old dog, old tricks

SOMETHING funny is happening to American broadcast television, which kicked off a new season this week. ABC, a network owned by Disney, has added four new sitcoms to its Wednesday evening prime-time schedule. More radically, NBC has replaced five hours of drama per week with Jay Leno, a large-chinned comedian. On Mondays, Wednesdays and Thursdays viewers will have the option of watching nothing but comedy on the four big English-language broadcast networks between 8pm and 11pm. Then it is on to the late-night and late-late-night comedy shows.

It is a partial reversal of a trend that seemed inexorable until recently. British and American broadcasters have lamented the slow death of comedy, especially the sitcom. Many creative explanations for its decline have been put forward, including simple fashion, multiculturalism and audience fragmentation eroding consensus about what is funny, and (in Britain) the alarmingly high bar set by "The Office", an acute satire about white-collar work that first aired in 2001.

ABC's new crop of comedies are what *Variety*, a trade magazine, calls "laffers". They are half an hour long and purely comic. By contrast, "dramedies" such as "Chuck" and "Ugly Betty" fuse comedy with more serious themes and are an hour long. One new show, "Hank", is so old-fashioned as to star Kelsey Grammer (pictured), a veteran of the genre, and is filmed with multiple fixed cameras in front of an audience.

A better explanation for the sitcom's revival is simply that television is cyclical. In the late 1990s the American broadcast networks went crazy for comedy, apparently giving shows to anybody who was able to secure a writing credit on a hit such as "Friends". The result was widespread failure and an abandonment of the genre in favour of reality television. But the strong survived and eventually prospered. CBS, which stuck with sitcoms when others had virtually abandoned them, has enjoyed several fair-sized hits. It is also cleaning up in the syndication market. Comedies repeat better than dramas and much better than reality television.

Another reason is cost. Comedies, which rarely feature stunts and explosions, can be cheaper to make than dramas. Traditional fixed-camera sitcoms are about one-fifth cheaper to make than "single-camera" comedies, which are filmed on location. And Mr Leno is extremely cheap. He has boasted that it is possible to make five episodes of his show for the price of one episode of a police drama. Even if it ends up attracting many fewer viewers than those police dramas, the trade-off may well prove worthwhile, particularly if advertising remains weak.

If comedy rises from the ashes it will not be the first time it has done so. The sitcom was widely believed to be dead in the early 1980s. Then along came "The Cosby Show".

InnoCentive

A market for ideas

Sep 17th 2009 | NEW YORK
From The Economist print edition

A pioneering “innovation marketplace” is making steady progress

A PROBLEM shared is a problem solved: that is the belief that inspired InnoCentive, a firm that describes itself as the “world’s first open innovation marketplace”. Conceived in 1998 by three scientists working for Eli Lilly, a big drug company, InnoCentive was spun off as an independent start-up three years later. It is based on a simple idea: if a firm cannot solve a problem on its own, why not use the reach of the internet to see if someone else can come up with the answer?

Companies, which InnoCentive calls “seekers”, post their challenges on the firm’s website. “Solvers”, who number almost 180,000, compete to win cash “prizes” offered by the seekers. Around 900 challenges have been posted so far by some 150 firms including big multinationals such as Procter & Gamble and Dow Chemicals. More than 400 have been solved. InnoCentive reckons the approach can work for innovations in all sorts of fields, from chemistry to business processes and even economic development. It has formed a partnership with the Rockefeller Foundation, a charity, to help solve problems posted by non-profits working in poor countries, with some initial success.

Forrester, a consultancy, studied a pilot partnership between InnoCentive and SCA, a Swedish maker of personal-hygiene products with over 50,000 employees and annual sales of €10 billion ($14.6 billion). It found that challenges posted by the firm generated an average return on investment of 74%, with a payback period of less than three months. Forrester also found cost savings, a faster research process and a more innovative culture.

SCA was attracted by the fact that InnoCentive took great care in managing the intellectual-property issues that result from its approach, and that it paid for results rather than mere effort. According to one SCA executive, the firm piloted the relationship by posting several chemistry challenges, “some of which worked and some didn’t.” Phrasing the challenge turned out to be key. Rather than posting a problem specific to the firm, SCA got much better results when it posed a general problem (how to make a material more absorbent, say). That way the potential network of experts was wider. So far the challenges have been small: the largest prize paid was $25,000. But SCA now expects to expand its use of InnoCentive into the mainstream of its innovation process.

InnoCentive recently raised a second round of venture capital to pay for what it hopes will be rapid growth. Sceptics worry that its success on incremental, scientific challenges may not extend to broader, more substantial innovation because the research culture in most firms is incapable of posing the right questions or knowing what to do with the sort of answers produced by InnoCentive’s solvers.

A recent innovation may help. Called InnoCentive@Work, this replicates the solver network inside a firm, so that challenges are first offered to “seeker” companies’ own employees. Only if they cannot help is the outside network brought into play. “Companies often don’t know how much they already know,” says Dwayne Spradlin, InnoCentive’s chief. An early challenge at one firm was to find a source of some data, which, it turned out, had already been acquired by another division.

One of the first firms to test the @Work model was InnoCentive’s mother ship, Eli Lilly. That firm is struggling: on September 14th it announced plans to shed 5,500 jobs. The fact that Eli Lilly is making ever more use of InnoCentive to drive innovation even as it is making cuts elsewhere proves that it pays, says Mr Spradlin.

Economist.com BUSINESS

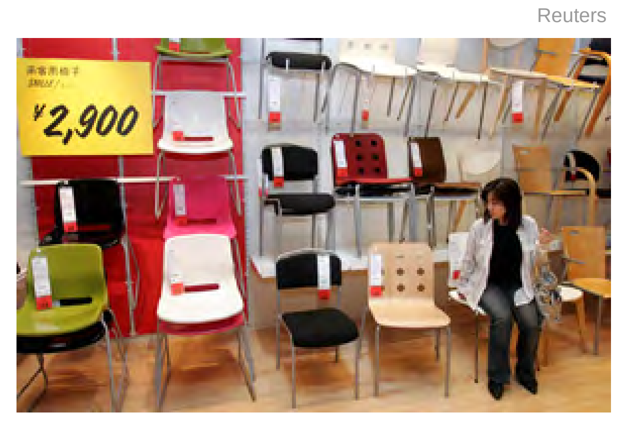
Consumer goods in Japan

Fashion victims

Sep 17th 2009 | TOKYO
From The Economist print edition

Beleaguered firms are merging at last—but cost-cutting is still taboo

Reuters



Why pay more if it's no more comfortable?

THE Japanese have long been tacit devotees of the old Gucci family motto: "Quality is remembered long after the price is forgotten." For years, no nation has spent more per person on luxury goods, nor been more disposed to pay the earth for a potentially deadly fishy delicacy. But something is awry in the land of mass luxury. The Japanese are finally, after an economic crisis that follows almost two decades of growing hardship, turning thrifty.

Even before exports collapsed last year, wages at the national level had begun to fall as well-paid elderly workers retired, to be replaced by underpaid youngsters. Now comes what Brian Salsberg of McKinsey, a consultancy, calls a fundamental shift in consumer behaviour. People are suddenly fighting for a good deal.

The response, as so often in Japanese business, is well-intentioned but a bit muddled. Feeble prospects at home help explain why Suntory, a firm familiar to foreigners as the maker of a single-malt whisky, has made a bid for Orangina Schweppes, best known for a fizzy orange drink beloved in France. Suntory was already in merger talks with Kirin, another Japanese drinks firm, which has acquired aggressively in Australia. Both firms hope their combined heft will help them move into China and other fast-growing markets. A potentially more tangible benefit of merger—cutting costs at home to boost profitability—is less discussed.

The same is true of the more defensive mergers on the Japanese high street. As sales of luxury goods have tumbled in the past year, there is barely an upmarket national department store that has not joined forces with a rival. But when *Nikkei*, a Japanese business newspaper, said last month that the newly merged Isetan Mitsukoshi, the country's largest department-store operator, planned to shed about 1,000 jobs as part of a cost-cutting drive, the company poured cold water on the report.

The episode underscored how hard it remains for Japanese companies to use cost-cutting as the logic for merging. Instead their primary focus is on driving top-line and market-share growth, says Steven Thomas, a mergers expert at UBS, an investment bank. Reducing overlaps is, at best, a secondary consideration. "It would get very exciting if a more cold-blooded attitude started to emerge," he says.

Yet not all are struggling. Some mid-market Japanese retailers, such as Uniqlo, a clothes store, and Muji, which sells everything from belts to bicycles, have retained an edge at home and expanded abroad. Online retailers are doing well. And where there were once slow-moving rivers of people only in Tokyo's fashion ghettos of Ginza and Omotesando, now you must fight through the crowds at determinedly cost-conscious foreign chains such as America's Costco and Sweden's H&M.

The latter's compatriot, IKEA, may be the best indication in Japan that people will still shop if the price is right. It abandoned Japan in 1986, owing to poor sales. When it returned three years ago, many doubted the hard-working Japanese would have the time, let alone the inclination, to spend weekends in flat-pack frustration. They were wrong. IKEA's sales in the year to August were up 44% from the previous year. That is another reason for the beleaguered incumbents to seek solace in each other's embrace.



Marketing on social networks

Friends for sale

Sep 17th 2009 | NEW YORK
From The Economist print edition

What is a Facebook friend worth?

ONLINE social networks are handy not just as a means of wasting time but also as a communications tool for business. Dell, a computer-maker, has made $3m in sales from Twitter since it started "tweeting" about its outlet that sells refurbished computers in 2007. Marketers are eager to use fast-growing networks to tout their products. An Australian online-marketing company, uSocial, wants to help them—for a price. On September 16th the firm started selling Facebook friends and fans.

After trawling Facebook for users by criteria like age, location and interests, uSocial then recommends potential friends to companies, who approach them directly. A firm pays $727 for each 5,000 users who agree to be its friend, or 15 cents each. "Fans", who merely express support for a firm, are cheaper.

It is not the first time uSocial has tried to sell the benefits of popular online destinations to marketers. It sells votes on websites such as Digg, which let people share content and vote on which articles should appear on the site's front page. It also sells Twitter "followers" (people who follow a user's updates) to companies looking for some positive buzz. Those websites disapprove. So does Facebook, which may try to bar uSocial from its service.

Social networks provide "the most powerful form of advertising there is", claims Leon Hill, uSocial's boss. But not everyone thinks uSocial's idea of selling friends makes for good marketing. Andrew Petersen of the Kenan-Flagler Business School at the University of North Carolina reckons that purchasing friends or fans does not establish brand loyalty and may actually hurt a firm's image by making it seem desperate.

Websites like Twitter and Facebook might lose some of their popularity if users feel they have become a forum for advertising rather than gossip. It is also in their interest to make sure uSocial does not claim profits that could be theirs. Facebook, which said on September 15th that it has 300m users, has struggled to make money from them. It recently launched a type of advertising that allows companies to target potential customers by letting users click on an advert to become that company's fan. The new offering from uSocial competes directly with this revenue source. No wonder uSocial does not have many friends of its own.

Halal food

Cut-throat competition

Sep 17th 2009 | PARIS
From The Economist print edition

Feeding Europe's Muslims is a growing business

Corbis



Better learn to spell it

JUST before the beginning of Ramadan, the month-long Muslim fast which ends this weekend, an unusual advertisement appeared on French television. Panzani, a pasta-maker, was touting its Zakia line of halal ready-meals. In a secular nation it seemed like "a little revolution", as *Le Parisien*, a newspaper, put it. The French can presumably take it in their stride. The trade in halal food is growing fast, and is likely to continue to do so.

Big food producers have long catered to Muslims, a market worth some $630 billion globally according to KasehDia, a consulting company that specialises in the trade. Nestlé has produced halal goods since the 1980s; 75 of its 456 factories now have a halal certification. But only recently have big European shops followed suit. Carrefour, the world's second-largest retailer, launched a new range of products just in time for Ramadan. Casino, a French supermarket chain, has a halal line, and British outfits Tesco and Sainsbury's carry halal products. KFC, an American fast-food chain, is conducting a trial of halal food in eight of its British restaurants. All its French ones are already halal certified.

The main reason for growth is demographic. Although many European countries do not tally Muslims or any other religious group (estimates in France range from 4m to 7m) it is clear that Muslim populations have grown quickly as a result of immigration and higher birth rates. Many of the people who sought asylum in Western Europe in the first half of this decade were Muslims from Afghanistan, Iraq and Somalia. Mohammed, Muhammad and Mohammad were all among the 100 most popular baby boys' names in England and Wales last year.

Although Muslims are disproportionately poor, they spend plenty of money on food. Islam is associated with a strong tradition of communal feasting. Antoine Bonnel, who runs the Paris Halal Expo, reckons that the average French Muslim spends a quarter of his or her income on food, compared with 12-14% for non-Muslims.

Nearly a third of the money goes on meat. That demand, which contrasts with a drop in meat-eating among health-conscious Christians and godless folk, has helped transform the global livestock market. The slaughtering of all lamb and goat meat in Australia for export is now done in accordance with halal custom, which involves killing animals with a single cut and draining their blood. A tenth of Australia's total meat exports, worth about $570m a year, is halal. Brazil dominates the global market with a 54% share of exported halal meat, according to KasehDia.

As the halal market grows, two problems are emerging. The first is the lack of broad standards. Halal regulations vary widely both between countries and within them. In Australia, all slaughter for halal meat is regulated by the government. In France, by contrast, there are over 50 certification bodies, all in competition with one another. Mr Bonnel describes it as "a huge nightmare" that can lead to charges of impurity. The Malaysian government's Halal Industry Development Corporation has tried to create a global standard, with little success so far.

The second problem is squeamishness among non-Muslims. Animals slaughtered according to halal custom are supposed to be alive when their throats are cut, a practice that animal-rights groups condemn. Switzerland, Norway, Iceland and Sweden forbid it outright. Some governments have reached a compromise that allows for animals to be partly stunned before being killed. But not all Muslims are happy with this. The halal market may be buoyant, but the waters are choppy.

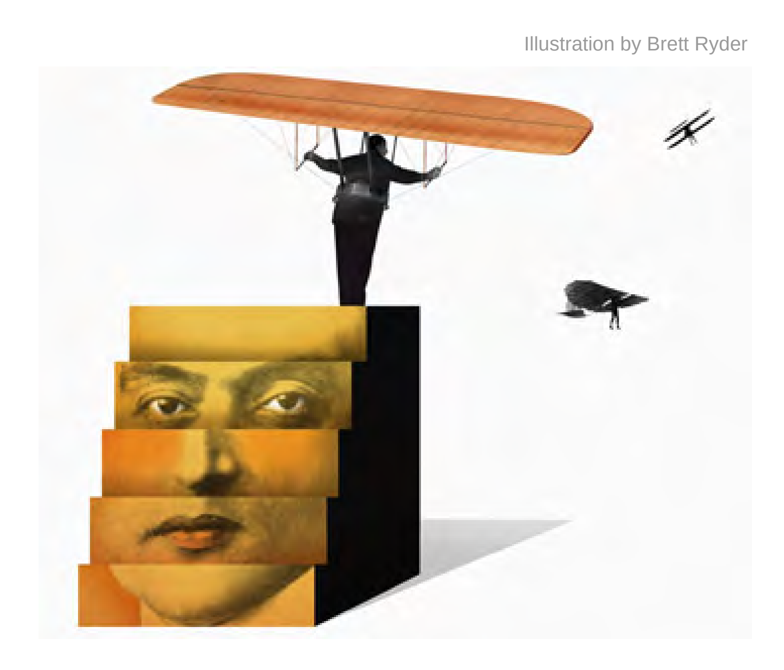
Schumpeter

Taking flight

Sep 17th 2009
From The Economist print edition

This week we launch a new column on business and management. Why call it Schumpeter?

Illustration by Brett Ryder



THERE is something about business that prevents most people from seeing straight. The rise of modern business provoked relentless criticism. Anthony Trollope featured a fraudulent railway company in "The Way We Live Now" (1875). Upton Sinclair dwelt on "the inferno of exploitation" in Chicago's meat packing industry in "The Jungle" (1906). Muckraking journalists denounced the titans of American business as "robber barons".

A striking number of business people accepted this hostile assessment. Friedrich Engels used some of the profits of his successful textile business to support Karl Marx, the self-proclaimed gravedigger of capitalism. Henry Frick's last message to his fellow steel magnate, Andrew Carnegie, was "Tell him I'll see him in hell, where we both are going." Many of the greatest business people threw themselves into philanthropy to try to win back the souls that they had lost in making money. Anti-business sentiment is still widespread today. For many environmentalists, business is responsible for despoiling the planet. For many apostles of corporate social responsibility, business people are fallen angels who can only redeem themselves by doing good works.

But anti-business sentiment is not as pervasive as it once was, thanks to the Thatcher-Reagan revolution and the collapse of communism. Instead there is new irritation to contend with—the blandification of business. Companies are at pains to present themselves as warm-and-fuzzy global citizens. Politicians praise businessmen as job creators. The United Nations and the World Bank celebrate businesses as all-purpose problem-solvers. Nicolas Sarkozy makes a distinction between business people (who create things) and financial speculators (who wreak havoc).

Joseph Schumpeter was one of the few intellectuals who saw business straight. He regarded business people as unsung heroes: men and women who create new enterprises through the sheer force of their wills and imaginations, and, in so doing, are responsible for the most benign development in human history, the spread of mass affluence. "Queen Elizabeth [I] owned silk stockings," he once observed. "The capitalist achievement does not typically consist in providing more silk stockings for queens but in bringing them within the reach of factory girls in return for steadily decreasing amounts of effort…The capitalist process, not by coincidence but by virtue of its mechanism, progressively raises the standard of life of the masses." But Schumpeter knew far too much about the history of business to be a cheerleader. He recognised that business people are often ruthless monomaniacs, obsessed by their dreams of building

"private kingdoms" and willing to do anything to crush their rivals.

Schumpeter's ability to see business straight would be reason enough to name our new business column after him. But this ability rested on a broader philosophy of capitalism. He argued that innovation is at the heart of economic progress. It gives new businesses a chance to replace old ones, but it also dooms those new businesses to fail unless they can keep on innovating (or find a powerful government patron). In his most famous phrase he likened capitalism to a "perennial gale of creative destruction".

For Schumpeter the people who kept this gale blowing were entrepreneurs. He was responsible for popularising the word itself, and for identifying the entrepreneur's central function: of moving resources, however painfully, to areas where they can be used more productively. But he also recognised that big businesses can be as innovative as small ones, and that entrepreneurs can arise from middle management as well as college dorm-rooms.

Schumpeter was born in 1883, a citizen of the Austro-Hungarian empire. During the 18 years he spent at Harvard he never learned to drive and took the subway that links Cambridge to Boston only once. Obsessed by the idea of being a gentleman, he spent an hour every morning dressing himself. Yet his writing has an astonishingly contemporary ring; indeed, he seems to have felt the future in his bones. The gale of creative destruction blew ever harder after his death in 1950, particularly after the stagflation of the 1970s. Corporate raiders and financial engineers tore apart underperforming companies. Governments relaxed their hold on the economy. The venture-capital industry exploded, the computer industry boomed and corporate lifespans shortened dramatically. In 1956-81 an average of 24 firms dropped out of the *Fortune* 500 list every year. In 1982-2006 that number jumped to 40. Larry Summers, Barack Obama's chief economic adviser, argues that Schumpeter may prove to be the most important economist of the 21st century.

A prophet and a role model

The prophet of capitalism's creative powers also understood the precariousness of the capitalist achievement. He pointed out that successful firms depend upon a complex ecology that has been created over centuries. He wrote extensively about the development of the joint-stock company and the rise of stockmarkets. He also understood that capitalism might be destroyed by its own success. He worried that a "new class" of bureaucrats and intellectuals were determined to tame capitalism's animal spirits. And he warned that successful business people were always trying to conspire with politicians to preserve the status quo.

Naming this column after Schumpeter does not imply that we endorse everything he said. His ideas about long business cycles have not withstood the test of time. He was too sceptical about the case for using government spending to avert depressions. He underestimated the self-correcting power of democracy. Moreover, this will be a column about business and management, rather than finance and economics. But the champion of innovation and entrepreneurship surely got as close as anybody to identifying what a column on modern business should be about.

Listen to a discussion about Schumpeter at Economist.com/audiovideo/business

Economist.com OPINION

LVMH in the recession

The substance of style

Sep 17th 2009 | PARIS
From The Economist print edition

The world's biggest luxury-goods group is benefiting from a flight to quality, but the recession is also prompting questions about the company's breadth and balance

Bloomberg



"THERE are four main elements to our business model—product, distribution, communication and price," explains an executive at LVMH, the world's largest luxury-goods group. "Our job is to do such a fantastic job on the first three that people forget all about the fourth." For decades LVMH's formula has worked like a spell: seduced by beautiful status-symbols, perfect shops and clever advertising, millions of people have swooned forgetfully towards the firm's cash registers. At Louis Vuitton, LVMH's star company, the model's pricing power has yielded consistent profit margins of around 40-45%, the highest of any luxury-goods brand.

These days customers are finding it far harder to forget about price. The seriously rich, of course, are still spending freely. But much of the industry's rapid growth in the past decade came from middle-class people, often buying on credit or on the back of rising house prices. According to Luca Solca of Bernstein Research, 60% of the luxury market is now based on demand from "aspirational" customers rather than from the wealthy elite. The recession has quickly reversed the trend to trade up, and people are delaying expensive purchases. Bain & Company, a consulting firm, expects the industry's sales to fall by a tenth in 2009, to €153 billion ($225 billion).

Some executives even expect a lasting shift in customers' preferences, towards discretion and value. Bernard Arnault, chairman and chief executive of LVMH, believes that the whole industry needs to rebrand itself. "The word luxury suggests triviality and showing off, and the time for all that has gone," he says. Brands which sold "blingy" easy-to-sell products, milking old names, he says, will fare particularly badly in the new environment. LVMH, by contrast, has never taken such an approach, he says, instead emphasising quality, innovation and creativity.

To underline these values, the group is going back to basics in its daily operations. "Before the crisis, we were putting a lot of energy into beautiful stores, but now we care a bit less about expanding our network and even more about design and price," says an executive. A few years ago, for instance, at the height of the boom, one LVMH brand was putting diamonds all over its watches, so that it was almost difficult to tell the time. "Now we are getting back to what really matters, which is nice movements and design," he says.

For some luxury firms, the recession's effects have already been brutal. Private-equity firms and other outside investors which rushed into the industry at its peak have suffered most. "At the top of the market this industry was perceived as easy by outsiders," says Mr Arnault. "You borrowed 80% of a target's asking price and hired a good designer, but the strategy has not been successful in several cases."

Lenders to Valentino, an Italian fashion house, are reportedly trying to renegotiate its debt. Permira, a private-equity group, bought the firm in 2007 in a deal valuing it at €5.3 billion. Permira has since written down its equity investment of about €900m by more than half. Prada Holding, through which Miuccia Prada and her husband control Prada Group, another Italian house, recently restructured its loans in order to defer payment to banks. Prada Group has denied that there are talks to bring in a minority shareholder. Two particularly weak firms, Christian Lacroix, a Paris-based ready-to-wear and haute couture label which used to be part of LVMH, and Escada, a German maker of luxury womenswear, filed for bankruptcy earlier this year.

Amid this turmoil, LVMH is performing relatively well (see chart 1). It has benefited from an established pattern in the luxury industry: when people have less, they spend what they do have on the best quality. Shoppers are going for fewer, classic items—one Burberry raincoat, rather than three designer dresses, or a single Kelly bag by Hermès, a French luxury-goods group, instead of four bags from various lesser designers. For this reason, says Yves Carcelle, chief executive of Louis Vuitton and president of fashion and leather goods for LVMH, "Vuitton always gains market share in crises."

Luxury's so last year 1

Selected luxury-goods companies

Revenue, H1 2009, % change on a year earlier

20 15 10 5 - 0 + 5 10

Richemont*

Swatch Group

PPR Group

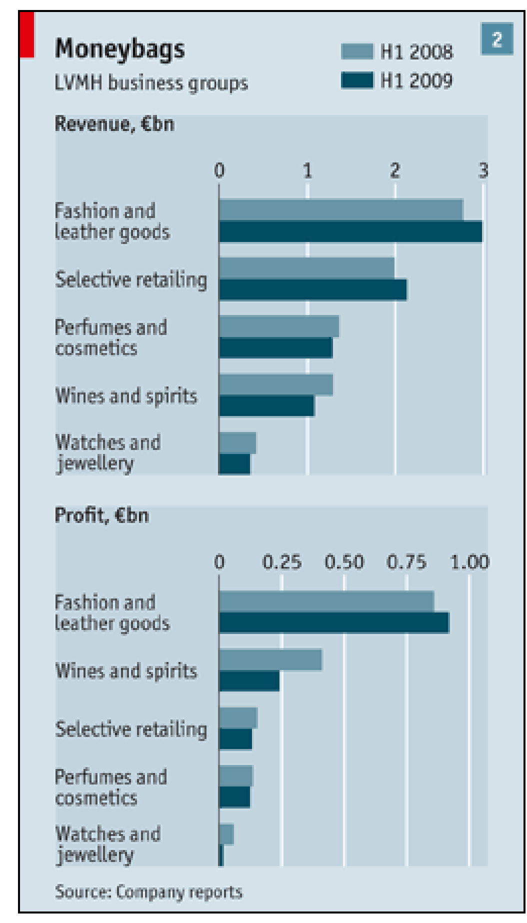
LVMH *nil*

Hermès Group

Source: Company reports *Five months to August

As reliable and sturdy as one of its own handbags, therefore, Vuitton is carrying LVMH fairly comfortably through the recession. In the first half of 2009 the group's revenues were about the same as a year before, though profits were 12% lower. Two divisions—wine and spirits, and watches and jewellery—were the worst affected: their revenues each fell by 17% and their profits by 41% and 73% respectively (see chart 2). Rapid de-stocking by retailers exacerbated the effect of falling demand. But the falls were offset by Vuitton, where revenue rose by a double-digit percentage, registering gains in every market. "It is incredible that in a downturn the consumer still buys so many Louis Vuitton bags, but she or he does," says Melanie Flouquet, luxury-goods analyst at JPMorgan in Paris.

Vuitton's performance, and the overall robustness of LVMH, a global conglomerate with more than 50 brands and revenues of €17.2 billion in 2008, should allow it to take advantage of its competitors' weakness in the recession. "In the next few years we expect several failures in the industry and good opportunities to acquire assets at attractive prices," says Mr Arnault. Shareholders in the firm are particularly preoccupied by what he might buy and sell in the next few years.



What explains Vuitton's resilience? Beneath the gloss of advertising campaigns, catwalk shows and each season's fleeting trends, Vuitton brings a machine-like discipline to the selling of fancy leather goods and fashion. It is the only leather-goods firm, for instance, which never puts its products on sale at a discount. It destroys stock instead, keeping a close eye on the proportion it ends up scrapping (which it calls the "destruction margin"). In 2005, when Maurizio Borletti, owner of several prominent department stores in Italy and France, was preparing for the opening of a refurbished La Rinascente department store in Milan, he recalls, the Vuitton people built a scale model of the building in their offices to understand customer flows and get the best positioning. "In this they're the most professional in the industry," he says.

Unlike most other luxury marques, Vuitton never gives licences to outside firms, to avoid brand degradation. Its factories use techniques from other industries, notably carmaking, to push costs down ruthlessly and to allow teams of workers to be switched from one product to another as demand dictates. It has adopted methods of quality control, too: one quality supervisor came from Valeo, a French auto-parts supplier. The result is long-lasting utility, beyond show, which is valuable in difficult times.

Owning shops gives Vuitton control over levels of stock, presentation and pricing. It was not therefore

affected by the panicked price-slashing of up to 80% by American luxury department stores in the run-up to Christmas last year—a "catastrophe" for others in the industry, according to Mr Arnault. Although other LVMH divisions have been hit by outside retailers de-stocking during the crisis, Vuitton has managed its own inventory, with no competition for space from other brands. With a global network, says Mr Carcelle, the firm can move poorly selling stock to shops where it has performed better.

The luxury of diversity

Vuitton's ability to offset the steep falls in other divisions shows the value of the diversified conglomerate model in luxury goods. Richemont, the industry's second-largest company, has a less varied portfolio and greater exposure to watches and jewellery, demand for which has been especially weak. According to a recent trading statement, its sales fell by 16% in the five months to the end of August.

A group structure also yields savings when negotiating deals for advertising space, property and credit-card fees. It helps to have a specialist beauty retailer, Sephora, and a chain of airport shops, DFS, to sell perfumes and cosmetics. When Vuitton develops watches, say, it can call on the talents of TAG Heuer. But LVMH's breadth also comes in for criticism. Although there is undoubtedly value in some diversification, some people ask whether 50-odd brands under one roof are too many. Vuitton, for instance, would doubtless like to see disposals of weaker brands as a result of the crisis, and a greater concentration of resources on the group's key businesses.

The group's executives devote the bulk of their attention to the most important of these: Louis Vuitton, Moët Hennessy in drinks, TAG Heuer in watches, Christian Dior in perfumes and cosmetics, Sephora and DFS. The group has many smaller businesses, and these get much less attention in such a big group. LVMH does not disclose financial figures for individual brands, but at its presentation of first-half results the group's finance director replied to an analyst asking about fashion and leather-goods that a "handful" had lost money "somewhere". There is speculation that Celine, a ready-to-wear clothing and accessories label, Kenzo, a fashion brand which analysts have long suggested LVMH dispose of, or Loewe, a Spanish leather-goods brand which has so far failed to win much of a following outside Spain and Japan, are among the less profitable.

Nevertheless, the group can use the might of Vuitton to support its smaller, upcoming brands. A department store, for instance, may be asked to take Loewe or Celine in order to get Vuitton. That often frustrates people at Vuitton, however, who would prefer to use the power of the brand for its own benefit, says a person who knows the company well. "They've never heard of another of LVMH's brands saying, 'Either give this to Vuitton or I won't come'," he says. Apart from the synergy in watch design, Vuitton does not find that it benefits much from the rest of the group.

The reason why LVMH has many small brands which aren't quite making it, says another person familiar with the company, is that Mr Arnault is an optimist who believes that every property can at some point be turned around. That can pay off: some years ago Mr Arnault halted the imminent sale of a make-up line. Thanks to the distribution muscle of Sephora, it has since turned into a bestseller in America. Investors, however, are nevertheless wary of what they see as Mr Arnault's tendency to collect brands.

The crisis has also underlined the fact that Vuitton dominates the group's results. Were it not for Vuitton, estimates one analyst, LVMH's sales would have fallen by 3% in the first half of 2009 and profits would have plunged by 40%. In normal times Vuitton contributes about half of the group's profits, and most of the rest comes from Moët Hennessy. In the first half of this year, however, Vuitton contributed an estimated 70% of profit. That leads some people to question whether LVMH is overly dependent on the leather-goods firm.

"You can argue that there's nothing as good as Vuitton in LVMH's portfolio," says Pierre Mallevays of Savigny Partners, who was formerly director of acquisitions at LVMH, "but that simply states the fact that LV's business model is the gold standard of luxury brands; no other brand in the world compares to it." The biggest risk to LVMH is Vuitton, argues Ms Flouquet, since it accounts for such a big proportion of profits; the company depends on it, she says. The risk to Vuitton, in turn, is that it could fall out of fashion or lose its exclusivity in the eyes of consumers.

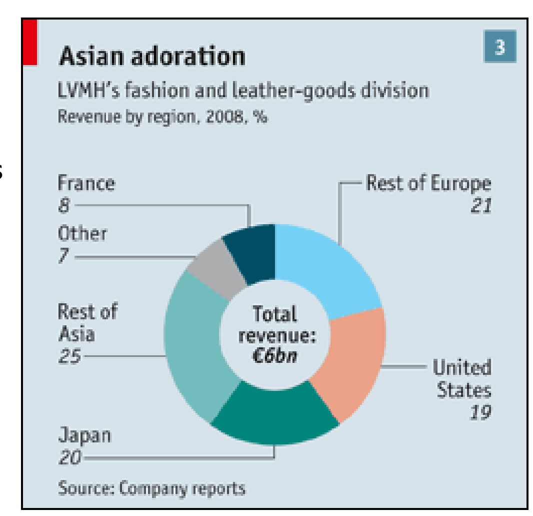
So far there is no sign of fatigue with the brand. LVMH's senior managers have devised ways to refresh it. In the late 1990s, for example, Mr Arnault saw that there was a risk that as a maker of leather goods alone, Vuitton could be perceived as boring. In 1997 he hired Marc Jacobs, then a relatively unknown designer, to design a fashion line. The aim was to generate seasonal buzz and press coverage. Vuitton's senior executives at the time were against the idea, fearing that adding fashion could undermine a

timeless image, but Mr Arnault's move proved successful.

To avoid overexposure of its signature "Monogram" print, Vuitton has taken care to develop a wide range of products and other patterns. "We increase the number of product lines and we are careful to have several different colours and shapes," says Mr Arnault. Thus Vuitton sells reasonably priced handbags—the smallest Speedy Bag costs €430 in Paris—but also wildly expensive custom-made luggage, reinforcing its exclusive image. Another effective tactic is to make limited-edition handbags which are hard to get hold of.

Five or so years ago Vuitton depended to a large degree on one market, Japan. Most Japanese women owned at least one Vuitton product—and hence provided a large proportion of Vuitton's profits, which worried analysts at the time. Yet the Japanese market for luxury goods was souring. Spending on such items in Japan has fallen sharply since the end of 2005, according to a recent report by McKinsey, a consulting firm. Young women are more individualistic than their mothers, and are seeking out lesser-known brands. "You used to see thousands of Vuitton bags coming at you in the Ginza shopping district but far fewer now," says Radha Chadha, author of a book, "The Cult of the Luxury Brand: Inside Asia's Love Affair with Luxury".

That reliance on one country is no longer so marked (see chart 3). Fortunately, Vuitton has since rapidly established a strong position in what it hopes will become another Japan: China. "The Chinese consumer is in a love affair with the Vuitton brand," says Ms Flouquet. According to LVMH, in the first half of 2009 sales to Chinese people (at home and travelling) made up 18% of Vuitton's revenue. Despite widespread concerns about counterfeiting in the country, the Chinese are now Vuitton's biggest customer base after the Japanese. The key to the firm's success, says Mr Arnault, has been approaching the market exactly as if it were a developed market. "We treat the Chinese customer as being very sophisticated." Many competitors, by contrast, have at times lowered their standards for shops in China, he says, using inferior furniture or positioning their stores poorly.



Going into new markets and developing new product lines will enable Vuitton to continue producing double-digit growth for years to come, says Mr Carcelle. On every trip to mainland China—he makes five or six a year—he tries to discover a new city and meet its mayor. Mr Carcelle is also tackling other new frontiers: in October he will open a shop in Sukhbaatar Square in Ulan Bator. "Already if you go to an upmarket disco in Ulan Bator you will see a significant number of our bags," he says.

Vuitton's expansion into China, Mongolia and new product lines such as watches and shoes, suggest that the leather-goods firm will continue to be LVMH's main source of growth. However, it also means that the group may become more rather than less reliant on Vuitton. In theory, the answer could lie in strengthening some of LVMH's smaller names, such as Fendi, a fashion and leather-goods brand. But buying a big, established, global brand with potential for growth could be both a quicker and a surer route.

ImagineChina

A new collection?

Analysts and bankers are convinced that Mr Arnault wants to buy the Hermès Group, a producer of leather goods and fashion which matches Vuitton for quality and design. Because Hermès is run so conservatively, says an investment banker who knows LVMH well, it is only a quarter of the size that it could be. "Mr Arnault would grow it while preserving its values," he says. Earlier this year, there were rumours that LVMH would sell Moët Hennessy to Diageo, the world's biggest spirits group, which already owns 34% of the business. Such a sale could raise money to buy Hermès. Mr Arnault, however, refuses to be drawn into commenting.

For the moment, such an acquisition is impossible, since the family which controls Hermès does not want to sell, and the firm is strongly defended against takeover. Nevertheless, says the banker, the family which controls it has several branches, all with different views. "It's a pressure cooker and

some day it will blow up," he says. Chanel, another closely held global luxury brand, could also make a desirable target for LVMH. Some people recommend a merger with Richemont, which, Mr Solca argues, would address LVMH's relative weakness in watches and jewellery.


Or maybe that one

Any such deals, or selling Moët Hennessy, would radically change the balance of the group. "I would be surprised if LVMH sold Moët Hennessy. The business has high margins, high cashflow and it is well managed," says Ms Flouquet. "They would probably only sell it if they had a large deal ahead." Shareholders are nervous that LVMH will pay too high a price for a large acquisition. For this reason the group's valuation may not fully reflect its performance during the crisis. Such concerns are not likely to deter Mr Arnault, who has demonstrated his confidence in LVMH's prospects in luxury by raising his stake in the group over time: he owns 47%. If LVMH does go shopping, it will probably behave like one of its best customers: with price in mind, but willing to spend on enduring prestige.

The IMF assessed

A good war

Sep 17th 2009 | WASHINGTON, DC
From The Economist print edition

The IMF has done well under Dominique Strauss-Kahn, but its future is unclear

AFP



DOMINIQUE STRAUSS-KAHN, the ebullient managing director of the International Monetary Fund, likens its role to that of a doctor. As the crisis has spread, the IMF has been called in to cure ailing economies from Ukraine to Pakistan. It is still too early to judge the success of the fund's prescriptions for troubled countries. But the IMF itself is certainly in far ruder health than it was at the start of the financial crisis.

Just a year ago the fund's finances were in tatters and its relevance was in doubt. During the early stages of an economic crisis that should have been its natural terrain, Barry Eichengreen, an economic historian at the University of California, Berkeley, wrote: "Global crises used to remind us why we have the IMF. If the fund doesn't come up with some new ideas for how to handle this one, the crisis may only remind us why we can forget it."

Part of the IMF's problem was that its reputation had been severely dented by the experience of rescue operations during the 1997-99 emerging-market crises, when it prescribed notoriously bitter fiscal and monetary pills. As a result its advice lacked legitimacy, particularly in emerging Asia, which saw the fund's views as geared to its rich-country backers in Europe and America. Many emerging economies subsequently concentrated on building up enormous foreign-exchange reserves to ensure that they would not have to turn to the fund again (these reserves are held by many to have been an underlying cause of today's crisis). That in turn meant that the fund had so little income from loans that it could not cover its costs.

Mr Strauss-Kahn himself had a difficult start when he took over as managing director in November 2007. His first big task was a contentious cull of around 15% of the staff. And just as the first group of crisis-hit emerging economies was turning to the IMF, an investigation into an affair between him and a member of staff proved an embarrassing (albeit brief) distraction. Few would have predicted at that point just how adroitly Mr Strauss-Kahn would move the fund back to centre stage.

The biggest sign of his success is a trebling of the IMF's kitty to $750 billion. Some of the new money has come from familiar sources such as America and Europe. But in a boost to the fund's legitimacy, the BRIC economies—Brazil, Russia, India and China—have all agreed to contribute to its coffers by subscribing to its first-ever bond issue, to the tune of $80 billion.

Equally important, the fund has been on the cutting edge of the global policy response. As Mr Strauss-Kahn puts it, the fund's experience of 122 earlier banking crises gives it "unparalleled expertise at the intersection of Main Street and Wall Street". He was an early, vocal and consistent advocate of co-ordinated global fiscal stimulus, advice that in hindsight seems remarkably prescient. And the IMF's analytical work—whether in identifying the scale of the losses from the financial meltdown or in predicting the effect of the crisis on public finances—has helped reinforce its intellectual credentials.

The extra cash has allowed the IMF to go into crisis-hit countries with packages that can make a difference. It has also allowed the fund to offer "crisis insurance" in the form of a new pre-emptive lending tool, the Flexible Credit Line (FCL). Mexico, Colombia and Poland have so far used this facility. And it still has more money available to lend than it did before the crisis.

The fund's standard crisis-mitigation loan packages have become more responsive to conditions in client countries. Mr Strauss-Kahn says that its use of conditions attached to loans has become more focused on "fixing the crisis, not fixing the world". He points to the removal of conditions related to land reform from the IMF package in Ukraine because, though useful, they were not essential for macroeconomic stabilisation. Insiders also credit Mr Strauss-Kahn with emphasising the need to protect spending on the very poor. His background in politics has made him keenly aware of the need to ensure that economic adjustment can work politically.

Despite having had a good run so far, the IMF's relevance once the crisis is over is far from assured. For his part, Mr Strauss-Kahn is nothing if not ambitious. He argues that the success of the FCL paves the way for the fund to become a true global lender of last resort, much as John Maynard Keynes originally proposed. For this to work, he believes that the IMF needs more money—perhaps as much as $2 trillion in all—and the trust of its poorer members, so that they rely on the fund's resources, rather than their own reserves, to insure against crises.

Gaining this trust will require reforms to the fund's "quotas" to give emerging economies more voting power. One round of changes has already been agreed, though not yet implemented. The G20 countries have asked the IMF to complete its next set of quota reviews by January 2011. But to satisfy developing countries, rich ones would have to give up more power than they may be prepared to. The finance ministers of the BRIC countries want a shift in voting power toward emerging countries that is considerably bigger than anything proposed so far.

To be useful, the IMF must also be ready to take unpopular positions. Mr Strauss-Kahn quotes Keynes when he promises that the fund's "ruthless truth-telling" will convince countries of the soundness of its advice. But more representative governance may make such candour more difficult. Some argue that the IMF has retreated from criticism of China's exchange-rate regime as China has become a bigger backer.

Keynes also envisaged the existence of sanctions for both surplus and deficit countries. But Mr Strauss-Kahn is wary of seeing the IMF as a sort of "policy police with legal instruments to make countries change their policies". Yet without some power to enforce its writ, the IMF is likely to be ignored, much as its advice on global imbalances was before the crisis. Like any good medic, the fund must find a way to strike a balance between being firm and being friendly.

Buttonwood

Alternative reality

Sep 17th 2009
From The Economist print edition

A wrongheaded fund-management directive from Brussels

Illustration by S. Kambayashi

“IT’S not fair.” That is the cry of children the world over when blamed by adults for some misdemeanour. And it is being echoed by private-equity and hedge-fund managers faced with the European Union’s proposed directive on “alternative-investment fund managers”.

The finance industry has two underlying suspicions, both of which appear to have some basis in reality. The first is that politicians who never liked the industry have seized on the crisis to impose restrictions, even though it was banks, not fund managers, that caused the damage. The second is that the French and Germans are pushing the legislation through as a way of undermining London’s dominance in financial services.

The industry’s unpopularity means it has to walk a fine line in its opposition. Complain too much and it risks being dismissed as a “bunch of whingers”. Complain too little and the directive may get bulldozed through. So the industry has to support general principles like openness and consistency while sticking the boot into proposals it does not like.



The first objection is that the directive has a “one size fits all” approach, even though the vehicles covered are very different. For example, the directive calls for independent valuation of assets. That might seem fair enough, given the scandals in which hedge-fund managers overstated returns. But private-equity managers are rewarded on the basis of realising assets. Only when portfolio companies are sold do investors get their money and managers get their performance fee. Having valuations in the interim, the industry argues, is a needless expense.

The second objection is that the directive seems to require everyone from managers through prime brokers to custodians to be based in the European Union. This is not about investor protection—investors want the best service provider, not just the local one. Poul Rasmussen, a former Danish prime minister and the driving force behind the directive, says the measure is “not protectionist”. But how he can say that is hard to understand.

The third problem is the lack of consistency. The directive requires private-equity managers to disclose details of quite small companies within their portfolios. But, the industry complains, the same level of disclosure is not required of companies run by families, Russian oligarchs or the subsidiaries of multinationals. That would seem to put private-equity groups at a disadvantage.

What really motivates the directive? It was clear, from remarks made by Mr Rasmussen at a debate in London on September 11th, that the industry’s critics dislike three things. Alternative-investment managers earn too much. They use too much leverage (in other words, they have risky balance-sheets) and are thus a threat to financial stability. And private-equity managers in particular are too keen on short-term profits at the expense of long-term investment and employment.

On the last point, academic studies have not proved a decisive case either way. But even if one accepts these criticisms at face value, they could surely be tackled more directly. If governments do not like people who earn too much, then they can raise taxes. As for the high level of fees, it may well be that alternative-investment managers enrich themselves rather than their clients. But since such clients largely comprise big institutions and the wealthy, they surely ought to be able to make such decisions for themselves. The hedge-fund industry has already shrunk significantly in the wake of the financial crisis.

If governments do not like companies taking on too much debt, they should stop making interest payments tax-deductible. In any case, the leverage available to hedge funds and private equity is largely a function of banks' willingness to lend. Higher capital requirements for banks should prevent a rerun of some of the recent excesses.

Indeed, the British regulatory system (London is where most European hedge funds are based) has worked pretty well. By focusing on the managers who run hedge funds, the system has so far avoided any major instances of fraud. By talking to prime brokers (the arms of banks that serve hedge funds), the authorities have also been able to monitor the aggregate level of hedge-fund exposure, and thus systemic risk.

In short, this is a pointless directive. The ever-sensible Swedes may smooth off some of the directive's rougher edges, but it is just luck that they are in charge of the EU at the moment. For once, the industry is right to complain.

Economist.com/blogs/buttonwood

Insider trading in Hong Kong

To the dungeon

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From The Economist print edition

Regulators are suddenly getting tough

AP



IT HAS long been considered a paradise for investors who have a juicy bit of inside knowledge. Insider trading was not even a criminal offence in Hong Kong until 2003. Earlier this year local tycoons banded together to block proposed changes to disclosure rules that, in effect, allow executives to front-run earnings announcements. So a striking change in regulatory approach has come as a shock to many.

Over the past year Hong Kong's Securities and Futures Commission (SFC) has initiated ten prosecutions for insider trading, resulting in ten guilty verdicts, dozens of convictions and five jail sentences. This month the SFC claimed its biggest scalp yet with the conviction of Du Jun, a former Morgan Stanley banker (pictured), who was expected to receive a hefty jail term at his sentencing on September 18th.

The SFC's harder line came about in a peculiar way, after what initially appeared to be a devastating setback. In 2008 an appeals court rejected two key powers of the government's insider-trading tribunals: their right to compel evidence and their right to assess fines beyond the repayment of ill-gotten profits. The ruling was part of a legal battle over the conviction of Koon Wing-yee, chairman of a firm called Easy Concepts, who was found guilty of tipping off a friend in 2000 about a takeover.

An initial consequence of the government's failure in the Koon Wing-yee case was to call into question the fines in 21 other cases (although ultimately no decisions were reopened). But the real significance of the appeal court's ruling was its opinion that punishment was rightly the prerogative of the criminal courts. Rather than be dismayed about this blow to its traditional legal venue, the SFC interpreted the ruling as a green light to skip the tribunals, where charges were heard as civil cases, and bring far tougher prosecutions. "Before, potential penalties were merely a fine and could be considered a cost of doing business," says Martin Wheatley, the SFC's boss. "Now they are a loss of freedom."

A series of cases, many of which had already been in the works, was quickly filed in criminal courts. Most involved small-time traders operating in tiny firms, but not all. One case involved leaks about a takeover by a vice-president at BNP Paribas (sentence: 26 months in prison for the employee, 12 months for his girlfriend); another involved tip-offs about a takeover from a director at CLSA, a regional stockbroking firm (sentence: six months in jail for the CLSA employee, 12 months for a fund manager). Mr Du was found guilty of buying shares in a firm at the same time as he was advising it on an acquisition.

Even these cases may pale in comparison with an ongoing investigation into Tiger Asia Management, an asset manager based in New York, some details of which were disclosed in a court filing last month. The SFC alleges that on January 6th Tiger was asked if it wanted to be among the buyers of shares in China Construction Bank (CCB). The shares were going to be sold by Bank of America, one of CCB's largest investors. The placement had obvious implications: a huge block of shares on the market would push prices down.

According to the court filing, Tiger responded to the invitation by quickly shorting CCB's shares before the offering was announced, and then covering its short position by participating in the placement. The transaction allegedly earned Tiger a rapid profit of HK$30m ($3.9m). Tiger could not have been the only firm notified about the share placement—Bank of America's stake in CCB was too large for a single firm to absorb, particularly at that crisis-infused time. Given broader price movements before that share sale and other placements, suspicions are rife that many hedge funds were using privileged information to front-run such offerings.

So far insider trading is not considered a serious enough offence to support extradition. Mr Du, who lives in Beijing, was arrested only when he was passing through Hong Kong's airport. But as a result of the Tiger filing, Hong Kong's regulators have sought to freeze the firm's assets in several (as yet undisclosed) foreign jurisdictions. Unlikely as it sounds, Hong Kong is gradually turning itself from a haven for insider trading into its scourge.

Investors and climate change

Green backing

Sep 17th 2009 | NEW YORK
From The Economist print edition

How can private capital be unlocked for green projects in poor countries?

NEITHER rich countries nor poor ones can tackle climate change alone. The rich bear most of the responsibility for the greenhouse gases in the atmosphere. But if they make cuts while the poor go on a carbon-heavy growth binge, the climate will suffer anyway. Rich-to-poor aid has thus been a big part of the discussions ahead of December's climate conference in Copenhagen, which is meant to hammer out a successor to the Kyoto protocol.

Public money will only go so far. The cash on the table for the rich world to help the poor world amounts to tens of billions—nowhere near enough to meet the needs of surging economies like those of China and India, which are both adding heavily polluting coal-fired power-stations at an alarming rate. Hundreds of billions will be needed for greener growth in this part of the world. How then to turn tens of billions of public dollars into hundreds of billions in private finance? Pension funds have a duty to guarantee their members' retirement benefits, after all, not cut carbon.

New thinking on this problem is emerging. In a forthcoming paper the World Economic Forum (WEF) suggests how public money can be used to guarantee, at least partially, rich-world investment in developing countries' greenery. Currency and political risk are among the factors currently keeping European pension funds, say, from investing in Indian renewables. The WEF calls for negotiations in which development banks—the World Bank or regional ones like the Asian Development Bank—would use public funds from the rich world to guarantee investors against these sorts of country risks.

Investors are also putting forward ideas of their own. On September 16th a group of 181 institutional investors, together representing $13 trillion in assets under management and including national, state and private pension funds, called on world leaders to agree stringent carbon-cutting targets at the Copenhagen meeting. Emissions must fall by 50-85% by 2050, said the group, and cap-and-trade systems like the one Europe has (and America's Congress is considering) must be a big part of the plan. Predictability of future policy is vital for these large, would-be green investors.

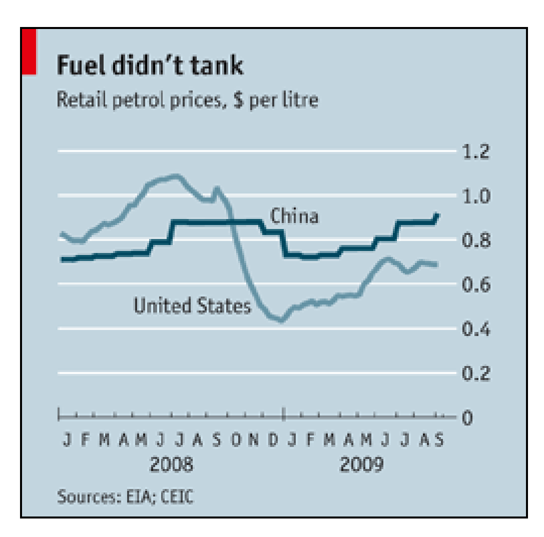
To turn private capital into green projects in the poor world, the group floated the idea of government-guaranteed bonds for climate-related investment, as well as more direct public support for specific green funds, in the form of loss-sharing agreements and debt guarantees. Some investors, like CalPERS, a huge Californian public pension fund, have already experimented with government-hedged green bets at a local level. Now to convince leaders to do it globally.

Petrol prices in China

Driving in the right direction

Sep 17th 2009 | HONG KONG
From The Economist print edition

Chinese motorists face unprecedented prices at the pump



ALTHOUGH crude-oil prices have bounced back since the start of this year, they are still only half what they were at their peak in July 2008—much to the relief of motorists worldwide. Americans, for instance, are paying one-third less at the pump than they did last summer. So why are Chinese drivers paying more for petrol than they did a year ago?

Earlier this month the government in Beijing increased petrol prices by 5%, to a record high. This was the seventh adjustment since January, when China introduced a new pricing system that allows local prices to track global crude-oil prices more closely than in the past. Petrol prices are adjusted whenever the average of a basket of international crude-oil prices rises (or falls) by a daily average of 4% over a 22-day period.

Last year, when crude-oil prices soared, Western economists heavily criticised China for holding petrol prices below market rates. Artificially cheap prices, they said, encouraged households and firms to guzzle more oil, pushing global prices higher. Low, government-fixed prices forced refiners to sell fuel below its international cost, causing big losses and widespread petrol shortages.

The government was reluctant to lift prices fully last year when inflation was already high, but it has taken advantage of domestic deflation this year to bring fuel prices more into line with world prices. In the summer of 2008 petrol was about 25% cheaper than in America. Now the average price in China is over 90 cents a litre, compared with only 69 cents in America (see chart).

Steps toward more market-based pricing are welcome, but the formula, which has not been published, is still being applied flexibly. The government says that price changes also take account of processing costs, profit margins and domestic supply and demand. If crude oil rises above $80 a barrel, not all the increase will be passed on.

Analysts reckon that the latest price rise was only half what it should have been if the price-setting formula were being followed precisely—probably to avoid upsetting consumers ahead of the 60th anniversary on October 1st of the founding of the People's Republic of China. Prices remain well below those in Europe: Germans, for instance, pay $1.85 a litre because of high fuel taxes. But Chinese motorists, facing record prices at the pump, may not be that grateful.

Economist.com FINANCE & ECONOMICS

Ireland's bad bank

The morning after

Sep 17th 2009
From The Economist print edition

Ireland’s toxic-asset plan makes a good fist of a bad situation

Illustration by S. Kambayashi



EVEN at the height of the boom, when bankers everywhere were partying harder than they should have been, those in Ireland were crowding the punchbowl like teenagers with no parents in charge. Instead of letting them suffer a painful hangover, the government has decided to hand over the analgesics.

On September 16th Brian Lenihan, the Irish finance minister, gave details of a plan to take bad loans with a face value of about €77 billion ($113 billion) off the balance-sheets of the country’s biggest banks. If the plan passes, these will go to a new agency, called the National Asset Management Agency (NAMA), in return for €54 billion in government-backed bonds.

The plan, so simple in theory, has proved fiendishly difficult to implement, not least because the government is trying to achieve three incompatible goals. The first is to restore trust in banks by cleaning up their books, so that the government can lift its blanket guarantee on their debts. Its second goal is to avoid enriching bank shareholders at the expense of taxpayers. And lastly it wants to do everything it can to avoid taking banks into state ownership. The trouble is that the banks have run up such large losses that it will be lucky to achieve even two of its three objectives.

Ireland has already shored up its banks once. In January it nationalised Anglo Irish Bank and injected €7 billion into Bank of Ireland and Allied Irish Banks, the country’s two biggest lenders. That recapitalisation was the equivalent of 4% of GDP and put the Irish bail-out roughly in line with those of most other developed countries. Yet it barely filled the hole in their books.

The IMF, which is forecasting a peak-to-trough 13.5% drop in Irish GDP by the end of 2010, reckons that the banks will post total losses of about €35 billion by the end of next year if they cannot offload their worst assets. Depending on when and where the remaining losses fall, some banks could be wiped out. Allied Irish and Bank of Ireland have but €22 billion in tier-one capital between them.

The unpalatable choice facing the government was deciding how much of the banking industry’s loss to inflict on bank shareholders and how much on taxpayers. The government seems to have erred on the side of favouring shareholders, largely to minimise the amount of capital it would have to inject into the banks. An average haircut of 30% on the assets’ nominal value still leaves banks with a hole to fill—on September 16th Allied Irish announced plans to raise €2 billion in capital. But NAMA will still pay about €7 billion more than the assets are actually worth.

Tweaking the plan further so that banks recognised even bigger losses upfront might have been more sensible for taxpayers. But were NAMA to pay the market value for the banks’ bad assets, then Irish banks would probably have to find as much as €7 billion in additional capital. Since equity markets might not oblige, that could require the government to stump up even more of its own cash to recapitalise the banks directly.

Despite its flaws, the NAMA plan seems like an advance over those in some countries—at least it gets something done. America’s scheme to buy toxic assets never got off the ground, while Germany’s bad bank is so punitive that most banks would rather stop lending than turn to it for help. The Irish government has also introduced some innovative risk-sharing elements to its plan. About 5% of the bonds NAMA will issue will be subordinated debt that will erode in value if the agency loses money.

Though Irish banks seem to be getting off lightly, that may not last. Patrick Honohan, the incoming governor of Ireland's central bank, is an expert in banking crises who has argued that holders of subordinated bank debt ought to suffer when banks fail. Among his published works is a 2000 paper for the World Bank on controlling the fiscal cost of banking crises. In it he argues authorities should take a "strict" approach to crisis resolution. The adults want to be back in charge of the punchbowl when the next party starts.

Morgan Stanley's head bows out

Mack moves on

Sep 17th 2009
From The Economist print edition

Bloomberg



Finance, like comedy, is all about timing. John Mack's was not always good. On returning to Morgan Stanley in 2005, he led a charge into hedge funds, housing and proprietary trading, increasing leverage in an effort to enhance returns. More forgivably, when markets crashed he cut the firm's risk-taking so sharply that it missed out on the bonanza as they rebounded. James Gorman, Mr Mack's anointed successor as chief executive, will on January 1st inherit a firm that has regained its poise but is still groping for a durable strategy. As he strives to find the right balance between its venerable but volatile securities business and its younger, more predictable retail brokerage, his predecessor will be on hand to offer friendly advice: Mr Mack is moving a few yards away, to the chairman's office.

Global house prices

It's life, Jim

Sep 17th 2009
From The Economist print edition

House prices are creeping up again. That may not last

THE latest survey of global house prices conducted by *The Economist* still makes for gloomy reading. Among the 19 countries we survey each quarter only Switzerland and China had housing markets that registered any increases in the 12 months to June. But the figures mask a modest recovery. In eight of the 16 surveyed countries for which quarterly data are available, house prices rose in the three months to June. Hong Kong and Australia led the charge, with prices rising by more than 4%.

The Economist house-price indicators
% change

	Latest	Q2 2008 on a year earlier	1997-2009*
Switzerland	4.6	2.7	27
China	1.0	9.2	na
Australia	-1.4	8.0	168
Sweden	-2.0	4.9	145
Britain	-2.8	-3.7	170
New Zealand	-2.8	-4.4	93
Italy	-3.4	4.3	99
Japan	-3.4	na	-35
South Africa	-3.5	5.1	380
United States *(FHFA)*	-4.0	-2.6	80
Canada	-4.1	3.9	63
Germany	-4.9	-3.2	na
Hong Kong	-5.3	25.6	-26
Netherlands	-5.6	1.8	93
Spain	-8.3	2.0	170
France	-9.3	3.0	128
Ireland	-12.5	-9.4	171
United States *(Case-Shiller national index)*	-14.9	-14.9	59
Denmark	-15.0	-1.7	90
United States *(Case-Shiller ten-city index)*	-15.1	-16.7	91
Singapore	-24.9	20.1	-17

*Or most recent available figure

Sources: ABSA; ESRI; Hypoport; Japan Real Estate Institute; Nationwide; Nomisma; NVM; FHFA; Quotable Value; Stadim; Swiss National Bank; Standard & Poor's; government offices

Interactive: Compare countries' housing data over time at: Economist.com/houseprices

In America the picture is murkier. The Case/Shiller national index of house prices rose by 2.9% in the second quarter, which was the first quarterly increase in three years. But other figures from the Federal Housing Finance Agency (FHFA), the regulator of Fannie Mae and Freddie Mac, two mortgage-financing agencies, showed a price decline of 2.4%.

Why the divergence? The FHFA index does not cover properties that have been financed by subprime loans or deals above the price cap for regulated mortgages. That excludes the bottom end of the market, where price falls have been much steeper and bottom-fishers have been lured back into the property game.

The FHFA numbers also strip out the top end of the market, where there are reasons to think that prices will stabilise more quickly. Banks are insisting on higher deposits from would-be homeowners, for instance, but such hurdles are less of an impediment for those with lots of cash on hand. Foreign buyers provide an extra source of demand for swanky properties. Stockmarkets roared back to life in the second quarter, too, which may have increased investors' risk appetite. Rising prices in higher-value properties, coupled with higher volumes in lower-priced ones, may be disguising stodginess in the middle of the market.

There are other caveats about the strength of a recovery. Governments are offering some short-term props to the market: first-time buyers in America are eligible for tax credits on deals that close before the end of November, for example. There are also fears of a new supply glut as owners are tempted by stabilising prices to put their homes back on to the market.

Mortgage rates are at historically low levels, which is helping buoy transactions, but if central banks begin to withdraw unconventional programmes to support the housing market, such as the Federal Reserve's purchases of mortgage-backed securities, the recovery may slow. That is in part because houses are still badly out of historical kilter with incomes, despite the price falls of the past two years. In Britain house prices remain 170% higher than they were in 1997, but average earnings have risen by only 55% in the same period. Steep declines in affordability have also taken place in Ireland, Spain and Australia.

Compare countries' housing data over time here

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Economics focus

Measuring what matters

Sep 17th 2009
From The Economist print edition

Man does not live by GDP alone. A new report urges statisticians to capture what people do live by

Illustration by Jac Depczyk



HOW well off are Americans? Frenchmen? Indians? Ghanaians? An economist's simplest answer is the gross domestic product, or GDP, per person of each country. To help you compare the figures, he will convert them into dollars, either at market exchange rates or (better) at purchasing-power-parity rates, which allow for the cheapness of, say, haircuts and taxi rides in poorer parts of the world.

To be sure, this will give you a fair guide to material standards of living: the Americans and the French, on average, are much richer than Indians and Ghanaians. But you may suspect, and the economist should know, that this is not the whole truth. America's GDP per head is higher than France's, but the French spend less time at work, so are they really worse off? An Indian may be desperately poor and yet say he is happy; an American may be well fed yet fed up. GDP was designed to measure only the value of goods and services produced in a country, and it does not even do that precisely. How well off people feel also depends on things GDP does not capture, such as their health or whether they have a job. Environmentalists have long complained that GDP treats the despoliation of the planet as a plus (via the resulting economic output) rather than a minus (forests destroyed).

In recent years economists have therefore been looking at other measures of well-being—even "happiness", a notion that it once seemed absurd to quantify. Among those convinced that official statisticians should join in is Nicolas Sarkozy, the French president. On September 14th a commission he appointed last year, comprising 25 prominent social scientists, five with Nobel prizes in economics, presented its findings*. Joseph Stiglitz, the group's chairman and one of the laureates, said the 292-page report was a call to abandon "GDP fetishism". France's national statistics agency, Mr Sarkozy declared, should broaden its purview.

The commission divided its work into three parts. The first deals with familiar criticisms of GDP as a measure of well-being. It takes no account of the depreciation of capital goods, and so overstates the value of production. Moreover, the value of production is based on market prices, but not everything has a price. The list of such things includes more than the environment. The worth of services not supplied through markets, such as state health care or education, owner-occupied housing or unpaid child care by parents, is "imputed"—estimated, using often rickety assumptions—or left out, even though private health care and schooling, renting and child-minding are directly measured.

The report also argues that official statisticians should concentrate on households' incomes, consumption and wealth rather than total production. All these adjustments make a difference. In 2005, the commission found, France's real GDP per person was 73% of America's. But once government services, household production and leisure are added in, the gap narrows: French households had 87% of the adjusted income of their American counterparts. No wonder Mr Sarkozy is so keen.

Sizing up the good life

Next the commission turns to measures of the "quality of life". These attempt to capture well-being beyond a mere command of economic resources. One approach quantifies people's subjective well-being—divided into an overall judgment about their lives (a "ladder of life" score) and moment-by-moment flows of positive and negative feelings. For many years researchers had been spurred on by an apparent paradox: that rising incomes did not make people happier in the long run. Recent studies suggest, though, that countries with higher GDP per person do tend to have higher ladder-of-life scores. Exactly what, beyond income, affects subjective well-being—from health, marital status and age to perceptions of corruption—is much pored over. The unemployed report lower scores, even allowing for their lower incomes. Joblessness hits more than your wallet.

Third, the report examines the well-being of future generations. People alive today will pass on a stock of exhaustible and other natural resources as well as machines, buildings and social institutions. Their children's human capital (skills and so forth) will depend on investment in education and research today. Economic activity is sustainable if future generations can expect to be at least as well off as today's. Finding a single measure that captures all this, the report concludes, seems too ambitious. That sounds right. For one thing, statisticians would have to make assumptions about the relative value of, say, the environment and new buildings—not just today, but many years from now. It is probably wiser to look at a wide range of figures.

Some members of the commission believe that the financial crisis and the recession have made a broadening of official statistics more urgent. They think there might have been less euphoria had financial markets and policymakers been less fixated on GDP. That seems far-fetched. Stockmarket indices, soaring house prices and low inflation surely did more to feed bankers' and borrowers' exaggerated sense of well-being.

Broadening official statistics is a good idea in its own right. Some countries have already started—notably, tiny Bhutan. There are pitfalls, though. The report justifies wider measures of well-being partly by noting that the public must have trust in official statistics. Quite so; which makes it all the more important that the statisticians are independent of government. The thought of grinning politicians telling people how happy they are is truly Orwellian. Another risk is that a proliferation of measures could be a gift to interest groups, letting them pick numbers that amplify their misery in order to demand a bigger share of the national pie. But these are early days. Meanwhile, get measuring.

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* "Report by the Commission on the Measurement of Economic Performance and Social Progress". Available at www.stiglitz-sen-fitoussi.fr.

Cleaning aircraft-cabin air

Breathing more easily

Sep 17th 2009
From The Economist print edition

The air inside aircraft could soon be cleaner and more comfortable to breathe

The air inside aircraft could soon be cleaner and more comfortable to breathe

Corbis



ONE concern of travellers is that flying can make you ill. Despite soothing reassurances from airlines that the air inside an aircraft's cabin is as clean as it can be, hundreds of people cooped up in a small space for a long time increases the risk of catching an infection. Viral diseases such as swine flu have spread quickly around the world by air. There are also pollutants to worry about: some airline staff claim to have been made seriously ill by engine fumes leaking into the cabin.

A new development could help passengers and crew breathe more easily. This week two British firms—BAE Systems, a defence and aerospace giant, and Quest International, a small producer of equipment used to sanitise the air in hospitals and nursing homes—announced that they had successfully adapted Quest's technology for use in aircraft. They make bold claims for AirManager, their new system. It can be fitted during a routine overnight service and uses less power than a light bulb, but is capable of zapping just about all the bacteria, viruses and other biohazards in cabin air—as well as destroying chemical contaminants and pollutants. And it also removes nasty smells.

Staying alive

Air has to be pumped into the fuselage of an aircraft once it flies above 3,000 metres (9,800 feet) because from there the air outside starts to become thin with too little oxygen to keep people alive. In the early days of commercial flight, when piston engines turned propellers, electrical generators were used to provide the power to pressurise the cabin. But with the arrival of faster, higher-flying jets, aircraft-makers found it more efficient to pressurise the fuselage by "bleeding" some of the air entering the compressor stage of the jet turbine (before it is mixed with fuel and ignited).

At first only fresh air was taken from the engines. But as jets have become more fuel-efficient, air bled from the engine has been mixed with recycled air from the cabin. This is because the big fans mounted on modern "high bypass" jet engines achieve thrust more efficiently by sending a larger volume of air around the turbine rather than through it. With less air available in the compressor, any that is bled off means the turbine has to work harder, which in turn increases fuel consumption. Typically an airline will strike a

balance by using a 50:50 mixture of fresh and recirculated cabin air, although pilots can reduce the amount of fresh air to save fuel. Some are thought to cut it back to only 20%.

The mixed air is maintained in the cabin at a pressure which is equivalent to an altitude of 2,500 metres and is passed through what are called high-efficiency particulate arrest (HEPA) filters. Provided they are well maintained, HEPA filters will trap most microscopic particles. But some things can get through, especially tiny viruses. The new AirManager system is said to kill 99.999% of pathogens in a single pass. Even on a short flight of about one hour, the cabin air will pass through the filters around 30 times.

David Hallam, inventor of the technology and a director of Quest, says the device works by generating a non-thermal plasma (sometimes called a “cold plasma”) using a high voltage to strip electrons from some of the molecules in a gas. The plasma is confined using an electric field and the cabin air is passed through it. The free electrons disrupt the molecular bonds of any particles in the air, causing them to break up into electrically charged pieces. An electrically charged filter then traps the bits like fly paper.

When Mr Hallam approached BAE to see if it could help adapt his invention for aircraft, some of the bigger company’s engineers were sceptical. But after four years of validation, BAE has been convinced. It has tested the AirManager with five European airlines that operate BAE’s small regional jet and recently obtained certification for an airline to fit the units to a Boeing 757. “There is a very tangible difference in the quality of air being breathed according to aircrew,” says Sean McGovern, who runs BAE’s regional-aircraft business.

The companies will now offer the system to operators of other Boeing and Airbus aircraft. Each unit costs about $16,000. Two are needed on a BAE regional jet and five on an aircraft like the 757. By allowing air to be recycled more safely, the devices could pay for themselves within a year by reducing the amount of engine-bled air that is needed and hence fuel consumption, says Mr McGovern.

Another advance that will make flying more comfortable in the coming years is the greater use of carbon fibre, especially by Boeing and Airbus, to make aircraft fuselages. Carbon fibre is stiffer than aluminium, which has long been used to make aircraft, and does not suffer from metal fatigue. One reason cabin pressures are kept low at the moment is to avoid stressing the fuselage too much. The use of carbon fibre will make it possible to pressurise cabins to a higher, more comfortable level.

Nor does carbon fibre corrode, so the air inside the cabin will not have to be kept quite so dry—which often leaves passengers with a wrung-out feeling after a long flight. And with recent advances in power electronics, Boeing has decided that it is now more efficient to go back to using electrical generators to pressurise the air in the cabin. This change will start with its forthcoming (and much-delayed) 787, which is supposed to fly for the first time by the end of the year. That will put an end to the trade-off between air quality and fuel consumption. As all these developments start to reach the market, passengers may start checking not just flight schedules and fares before booking a journey but also their airline’s cabin-air quality.

Exercise and company

Fitter with friends

Sep 17th 2009
From The Economist print edition

Exercising in a group can be more effective by making things easier

Getty Images



All together now

THE enduring image of Sylvester Stallone's legendary pugilist Rocky Balboa is that of a solitary athlete, braving the elements (and his own demons) to prepare for a fight. Yet according to a new study he might have done better by having a bit of company on his long workouts.

Research by Emma Cohen, an anthropologist at Oxford University, suggests that a better model is provided by Hicham El Guerrouj, a Moroccan middle-distance runner who is the current holder of the world 1,500-metres and one-mile records. Before retiring in 2006 Mr El Guerrouj was known for the throngs of training partners that followed him everywhere in Morocco. This was a good strategy because, as Dr Cohen reports in a forthcoming issue of *Biology Letters*, training in a synchronised group may heighten tolerance for pain. That, in turn, could allow athletes like Mr El Guerrouj to train longer and harder.

The reason is almost certainly the effects of endogenous opioids, better known as endorphins. When these are released in the brain they make a person feel good. What causes their release is more complex. Biologists think it is part of an evolved mechanism which rewards behaviour that may not be immediately pleasant but is ultimately useful to the species.

Endorphins show up nearly everywhere. Hunting an animal may be tiresome but necessary, so endorphins are secreted during exertion to numb the discomfort induced by lactic acid production in the muscles. Collaboration makes it easier to kill animals while others set traps.

Dr Cohen wanted to see if combining exercise and collaboration would heighten the effect. One of the study's co-authors, Robin Ejsmond-Frey, rowed for Oxford and thought it would be a good activity to study. For one thing, it is easy to spot a crew that is not well synchronised. Secondly, ergometers (machines on which rowers train) provide data on the power exerted on each stroke. And it can be rather painful so the endorphins should be out in droves.

The researchers got 12 members of Oxford's heavyweight squad to row on machines in four 45-minute sessions over two weeks. In two sessions they rowed in complete isolation and in the others in groups of six, perfectly synchronised. Immediately following each session their endorphin levels were tested. Because endorphin levels can only be measured directly through an invasive lumbar puncture—unfeasible, even for notoriously pain-hungry oarsmen—the researchers used a readily accepted proxy: they deduced pain tolerance, and hence endorphin levels, by gradually tightening a cuff around each rower's arm. When he said "now" they stopped squeezing and noted the pressure.

As expected, the rowers' pain thresholds were significantly higher following the group sessions. This was despite nearly identical power outputs in all four tests and efforts to control for possible confounding variables, such as the time of day.

The athletes may be rewarding themselves for their collaboration. Whether heightened tolerance is due specifically to rowing synchronously remains unclear. Data from other studies suggest that co-ordinated physical exercise can heighten social bonds (as in military training). The reverse may also be true. As the rowers had been teammates for nearly a year it is possible that the mere presence of friends explains the observed effect. The researchers are keen to replicate the study to test for such things. Meanwhile, solitary joggers might want to take along a friend or two.

Unhealthy showers

The joy of bathing

Sep 17th 2009 | NEW YORK
From The Economist print edition

A new study finds that nasty bugs can live in showerheads

IT HAS long been known that the air and water encountered by people in their daily lives are filled with all sorts of micro-organisms. Thankfully, most of these are benign and even the unsavoury ones can usually be washed down the drain without causing any harm.

Not always, though. A team of researchers led by Norman Pace of the University of Colorado at Boulder reports in *Proceedings of the National Academy of Sciences* that taking showers can pose a danger to some people. They took samples of the biofilm that builds up inside showerheads from 45 sites in nine American cities and analysed the genetic material which it contained.

Strikingly, in some of the samples they found high concentrations of a microbe known as *Mycobacterium avium* (a relative of the one that causes tuberculosis) which can cause respiratory illnesses. This is found in tap water, but remains harmless unless turned into an aerosol and inhaled—precisely what happens when bug-laden water is forced at high pressure through a showerhead. As the tiny particles are inhaled, they get into the lungs and can start an infection.

Is this cause for alarm? Not for healthy people, insists Dr Pace, but those with a compromised immune system or who are at risk of pulmonary diseases—the elderly, say—may want to take precautions. Cleaning showerheads with bleach will not do since the microbes will simply return with a fresh flow of water.

Replacing bug-prone plastic showerheads with metal ones is a good idea. So too, says Dr Pace, is letting the water flow for a bit to get rid of some of the gunk in the showerhead. But that would still leave one exposed to the aerosols formed by the fresh flow of water. The safest option for those at high risk might simply be to have a bath instead.

Rogue waves

Monsters of the deep

Sep 17th 2009
From The Economist print edition

Huge, freak waves may not be as rare as once thought


Science Photo Library

ON JULY 26th 1909 the *SS Waratah*, en route to London from Melbourne, left Durban with 211 passengers and crew. She was due in Cape Town three days later but never arrived. The steamship was last sighted along the east coast of South Africa—known to sailors as the "wild coast" for its violent weather—struggling through a stormy sea with waves more than nine metres (30 feet) high. No trace of the vessel has ever been found.

A theory which might explain her disappearance, and that of some other vessels, is that they were struck by rogue waves—which begin with a deep trough followed by a wall of water the size of an eight- or nine-storey building. For many years oceanographers dismissed sailors' reports of rogue waves much as they did stories of mermaids. But in 1995 an oil rig in the North Sea recorded a 25.6-metre wave. Then in 2000 a British oceanographic vessel recorded a 29-metre wave off the coast of Scotland. In 2004 scientists using three weeks of radar images from European Space Agency satellites found ten rogue waves, each 25 metres or more high.

A typical ocean wave forms when wind produces a ripple across the surface of the sea. If the wind is strong, the ripples grow larger. A hurricane can amplify a wave to a few storeys. But trying to create giant rogue waves in a laboratory tank is very difficult, making them hard to study. Now researchers led by Eric Heller of Harvard University and Lev Kaplan of Tulane University, New Orleans, have started using microwaves rather than water waves to create a laboratory model.

Rogue waves are not tsunamis, which are set in motion by earthquakes. These travel at high speed, building up as they approach the shore. Rogue waves seem to occur in deep water or where a number of physical factors such as strong winds and fast currents converge. This may have a focusing effect, which can cause a number of waves to join together. Such conditions exist along Africa's wild coast, where strong winds blowing from the north-west interact with the swift and narrow Agulhas current flowing down the coast to produce enormous waves. Dr Heller, who likes to sail, says there may be other mechanisms at work too, including an interference effect that causes different ocean swells, travelling at different speeds, to add up to produce a rogue, and a non-linear effect in which a small change in something like wind direction or speed causes a disproportionately large wave.

To study the phenomenon the group created a platform measuring 26cm by 36cm on which they randomly placed around 60 small brass cones to mimic random eddies in ocean currents. When microwaves were beamed at the platform, the researchers found that hot spots (the microwave equivalent of rogue waves) appeared far more often than conventional wave theory would predict; they were between ten and 100 times more likely.

Dr Heller says the results tend to support anecdotal evidence from seamen that rogue waves are not as rare as once thought. He thinks the work could also be used to understand more about the formation of these dangerous waves, perhaps to the point where it would one day be possible to provide a warning in places where rogue waves may be prone to appear. Seafarers would be thankful for that.

Teenage sexual maturity

Daddy's girl

Sep 17th 2009
From The Economist print edition

A non-obvious explanation for why girls without fathers have sex earlier

IT HAS long been a puzzle that girls who grow up without their fathers at home reach sexual maturity earlier than girls whose fathers live with them. For years, absent fathers have taken the blame for this, because growing up quickly has negative consequences for girls. For example, early-bloomers are more likely to suffer depression, hate their bodies, engage in risky sex and get pregnant in their teen years.

It could be a simple matter of not having as many eyes, particularly suspicious fatherly ones, watching over daughters. Or it could be a complicated physiological response to stress, in which girls adapt their reproductive strategy to their circumstances. If life is harsh, the theory goes, maybe they need to get their babies into the world as quickly as possible.

The animal world suggests that the effect is not restricted to humans. Young mice, pigs, goats and even a few primates get signals from their kin which inhibit sexual development; a strange male in their midst, by contrast, really speeds things up. Research in humans has shown that girls growing up with stepfathers mature even more quickly than fatherless girls and that stepbrothers have a measurable effect too. However, Jane Mendle of the University of Oregon and her colleagues have suggested another putative cause: genes. Specifically, the same genes that might make a dad more likely to leave his family could be behind early sexual development as well.

The researchers came to their conclusion after analysing data collected through the American National Longitudinal Survey of Youth. Dr Mendle looked at 1,382 boys and girls, each of whom was related to at least one other subject through their mother. Most of the mothers were pairs of sisters, but some were identical twins or first cousins raised as sisters.

The NLSY surveys asked the mothers about many things, including whether the father of their children lived with them. They were surveyed every year from 1979 to 1994 and then every second year. From age 14 their children were given annual questionnaires, and asked if they had engaged in sexual intercourse yet.

What the researchers wanted to know was whether the age at which a young person first had sex was something that ran in the family—regardless of whether the father had been around or not. To find out, they compared young people who had grown up without their dads with cousins whose dads remained at home. If the environmental effect of a father's absence was causing children to mature faster, they reasoned, that would show up.

It didn't. In fact, the more closely related the cousins were—by having mothers who were identical twins, for instance, versus cousins—the closer their age at first sexual experience, says Dr Mendle. The researchers found it was as true for boys as it was for girls. They published their work in the current issue of *Child Development*.

Dr Mendle now suspects that the same genetic factors that influence when a child first has intercourse also affect the likelihood that they would grow up in a home without their dads. What kind of genes could cause both? They could be ones that predispose a person to impulsivity, for instance, or sensation seeking. Or they could simply be genes that cause early puberty, suggests Dr Mendle—leading to early sexual experimentation, unintended pregnancy and a partner you never really chose and do not want to spend your life with.

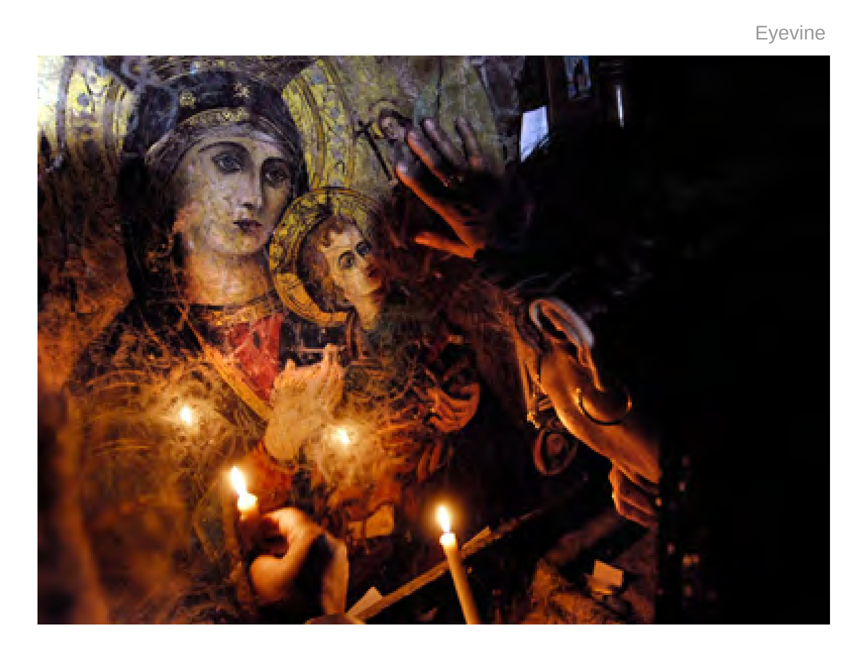
A history of Christianity

The greatest story, or the trickiest?

Sep 17th 2009
From The Economist print edition

Two books reveal the challenges of chronicling religious history

Eyevine



A History of Christianity: The First Three Thousand Years. By Diarmaid MacCulloch. *Allen Lane; 1,184 pages; £35. To be published in America by Viking in March 2010*. Buy from Amazon.co.uk

The Case for God: What Religion Really Means. By Karen Armstrong. *Knopf; 432 pages; $27.95. The Bodley Head; £20*. Buy from Amazon.com, Amazon.co.uk

A PROBLEM arises in any attempt to describe the whole of Christian history. From "inside"—in other words, for somebody who sees the story as a providential unfolding of God's relations with man—it is possible to construct a single narrative, albeit one that outsiders would find skewed. From "outside" the historian faces a problem of meanings and cohesion. Whatever a "bishop" was at Christianity's dawn, he was something different from the princes of the medieval church, and different from Rowan Williams, today's top Anglican. It is not just a matter of marshalling facts, but a question of seeing what, if anything, holds the story together.

So for Diarmaid MacCulloch, an Oxford don who specialises in the Reformation, the challenge of chronicling Christian history in just over 1,000 pages is manifold. His narrative may not quite hold together, but it has very good bits.

During the period he knows best, it is hard to distinguish Christian history from European history. Since Europe's wars were mostly fought in Christianity's name, there is no bright line between the sacred and the secular. Mr MacCulloch describes the era with a skilful sweep, though little distinguishes this section from a more general account.

Some will be less happy with his treatment of Christianity's early years, when basic doctrines were being hammered out. To this era Mr MacCulloch brings some baggage, and it can get in the way. A vicar's son, he was ordained as a deacon but declined to become a priest in protest against a homophobic wave that gripped the Church of England in the 1980s. (He has been active in the gay Christian lobby.) More than once he makes the point that in telling the story of self-described Christians, one must look beyond texts by early Christian writers whose main purpose was to denounce heresy. Fair enough, but such is Mr MacCulloch's preference for the heretical over the orthodox that a reader who relied on him alone might struggle at times to work out what the mainstream Christian view was, despite learning lots about those

who were against it.

Take one example: the Christian tradition—to which hundreds of millions of Catholics, Orthodox and Anglicans are heirs—holds dear the belief that Jesus Christ was both fully man and fully God, a single person with two natures, divine and human. It is a belief that generations of Christians have wept over, experienced mystically and died for. But Mr MacCulloch devotes little space to that teaching, and many pages (complete with his own misleading terms) to those who rejected it.

He is better at describing the political and military uses of religion than religion itself. In writing of the Christian East, he makes good points about religious nationalism in the post-Ottoman world. But he stumbles in explaining the medieval split between East and West over mysticism.

Mr MacCulloch copes better with the challenges of writing about modern Christianity, relegated to the margins of social, political and scientific developments. Church leaders, conscious that the world can do without them, have had to act nimbly and tactfully if they were to have any influence at all. Mr MacCulloch's tone changes sharply at this point, becoming lighter and more gossipy. He brings an insider's wit to tracing the fate of official Christianity in an age of doubt, and to addressing modern surges of zeal, from Mormons to Pentecostals.

To work really well, a grand history of a religious tradition has to blend an account of the faith itself with the ways this faith has influenced behaviour and the various historic conditions in which it has been articulated. Karen Armstrong is a good blender, which has made her a successful ambassador of religion in a generally irreligious age. In over a dozen books she has delivered something people badly want: a way to acknowledge that faith can be taken seriously as a response to deep human yearnings without needing to subscribe to the formality of organised belief.

Despite the title, her latest book is not so much a case for God as a case against atheism. Those who do not already have faith will not come away with a logical reason to believe. But she argues that modern atheism is as one-dimensional and transient a phenomenon as the modern varieties of theism (including fundamentalism) to which it responds. She praises the best of contemporary theology for the way it manages, like the mystics of early Christianity and Islam, to stress the limits of human discourse in addressing the divine.

But she, like Mr MacCulloch, has baggage. An ex-nun, she too is "on the rebound" from old-time Christianity, and she deals more ruthlessly than he does with the classical axioms of faith. She insists that Jesus of Nazareth made no claim to be divine: a famous New Testament passage that expounds both his self-abasement and divine glory does not mean what Christians think it means, she adds.

Ms Armstrong has won admiration from Muslims and Jews for expounding their traditions in ways that earn respect from outsiders. But such is her animus against traditional Christianity that she cannot render quite the same service for the faith she was once devoted to. This is a shame, not just for Christians but for secular readers too. Perhaps one day an interesting history of Christianity will be written by somebody who is neither a Christian nor an ex-Christian.

Harold Evans's newspaper memoirs

A golden age

Sep 17th 2009
From The Economist print edition

The Times



Ink on his hands

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SIR Harold "Harry" Evans remains one of the great figures of modern journalism. For this reason, and because the kind of campaigning, reporting-based work he stood for is threatened as never before, his autobiography, written as he turned 80, is both gripping and timely.

The book opens with an account of Sir Harry's rise from an upper working class home in Manchester. After an early setback of failing his 11-plus exam, his story is one of relentless ambition and determination. He left school at 16 to become a cub reporter on a local weekly. In love with journalism, he started a newspaper for the 800 men stationed with him in Wiltshire while doing his national service in the RAF.

Returning to civilian life in 1949, Sir Harry attended a lecture by a rather condescending executive (your reviewer's father) from the ineffably superior *Manchester Guardian*, who grandly informed his audience that it was not possible to explain world events without a knowledge of politics and economics gained from reading the likes of Macaulay and Keynes. Inspired, and against considerable odds, Sir Harry wangled himself a place at Durham University. With a degree came the offer of a job at the *Manchester Evening News*, then one of the country's most powerful provincial newspapers and, with its eight editions every weekday, one of the most demanding. It was here that Sir Harry acquired his hallmark virtuosity in almost every aspect of newspaper production. From reporting to editing to layout, there was no newsroom job he could not do.

A two-year break travelling America on a Harkness scholarship might have resulted in a career change. But at 32 he returned to England and was offered the editorship of the Darlington-based *Northern Echo*, a somewhat dated paper that still sold 100,000 copies daily across north-eastern England. Sir Harry speedily re-energised it with a revamped design, sharper reporting and editorials that addressed local issues. But what probably caught the eye of Denis Hamilton, the successful editor of the *Sunday Times* in London, was Sir Harry's flair for investigative and campaigning journalism. The young editor bravely ran national campaigns in his regional paper when he believed there was a wrong to be righted. His battle to force a reluctant health service to introduce countrywide screening for cervical cancer may have helped save the lives of thousands of women.

Hamilton brought Sir Harry to the *Sunday Times* and soon after, in 1966, made him his successor. Highly profitable, with a circulation of over a million and a formidable editorial staff, the *Sunday Times* was a wonderful stage for Sir Harry to perform from. He was also fortunate in his proprietor, the Canadian Lord (Roy) Thomson, who was steadfast in his belief that readers would pay for independent journalism.

Sir Harry quickly founded a full-time investigative unit to expose important scandals and carefully reconstruct major events. He believed teams were the key to investigative work because they enabled journalists to follow many trails (some inevitably false) and deploy a wide range of expertise in often technical material. A team is also likely to be more dispassionate than a single reporter on a mission.

Recalling his 14 years at the *Sunday Times*, Sir Harry gives compelling accounts of big stories, such as the paper's unmasking of Kim Philby's full damage as a spy; its noble campaign to win decent compensation for the victims of Thalidomide; and its efforts to report what was happening in Northern Ireland at the height of the Troubles, from the treatment of internees to the shootings on Bloody Sunday. Such stories involved long, costly and wearying challenges to political and legal authority. Writing about the Thalidomide affair, for example, often meant hazarding a jail sentence or a heavy fine for contempt. These were risks that Sir Harry bravely took, changing the law in the process. The paper "had to be ready to commit the resources for a sustained effort," he says of its lengthy investigations. "No campaign should be ended until it had succeeded—or was proved wrong." He left his beloved *Sunday Times* in 1981 after the paper and its daily sister were bought by Rupert Murdoch's News International. Persuaded to take up the editorship of the *Times*, he soon found himself butting heads with Murdoch executives. But his passion for anti-establishment causes made him a fish out of water there regardless.

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The queen mother

Doomed to repeat

Sep 17th 2009
From The Economist print edition

Queen Elizabeth the Queen Mother: The Official Biography. By William Shawcross. *Macmillan; 1,096 pages; £25. To be published in America by Knopf on October 20th*. Buy from Amazon.co.uk

Rex



Which way to the pub?

LIKE the Bourbon royal house of France, Britain's Windsors could be said to have "forgotten nothing and learned nothing". William Shawcross's lively and elegantly written biography tells the story of a charming though ill-educated young British aristocrat who was plucked from obscurity and wedded to an insecure royal prince—one who had previously been involved with a married woman and who was deeply uncertain about his suitability to be king. This young woman had beautiful eyes, a winning smile and a way with the elderly and the sick. But this is not the story of Diana, Princess of Wales. Rather, it is of an earlier inauspicious marriage, that of Queen Elizabeth the queen mother, consort of King George VI, late mother of Queen Elizabeth II and grandmother to Prince Charles.

Readers will search greedily for such parallels, and Mr Shawcross discreetly indulges. So it seems remarkable that the queen mother did nothing to stop the disastrous match between her grandson and Diana, the granddaughter of her old friend and lady-in-waiting, Ruth, Lady Fermoy. Indeed, she welcomed it, with fingers crossed. She never liked to acknowledge, let alone confront, disagreeableness within her family. This characteristic earned her the nickname "imperial ostrich" among some members of the royal household. "She thought her role was not to try and change people's courses but to be an anchor," Mr Shawcross writes.

She had always been an anchor. Lady Elizabeth Angela Marguerite Bowes-Lyon—the ninth of ten children borne by a Scottish laird, the Earl of Strathmore—was born in 1900. When she died she was nearly 102. She had never expected to become queen of England, and she did so in especially troubling circumstances. Her husband assumed the throne in 1936, after King Edward VIII abdicated in order to marry Wallis Simpson, a twice-divorced American. The second world war soon followed and proved to be the making of her.

Mr Shawcross, a former journalist and biographer of Rupert Murdoch, offers no big revelations about the queen mother. But he has had unrestricted access to her personal papers, letters and diaries, and he has mined them diligently. The result is a rich portrait of a woman who devoted herself to her duties and to bolstering her nervous husband and soothing his rages, known as "gnashes". She helped him overcome a stammer that had convinced his father, the irascible and demanding King George V, that the boy would never amount to much; and she comforted him after each bout with his older brother, who was enraged that his beloved Wallis was never accorded the title of Her Royal Highness. (Indeed, the queen mother studiously avoided her sister-in-law for decades.)

Although the book is too heavy to hold comfortably for long, Mr Shawcross is right to have quoted extensively from her private letters, which reveal her anguish over the abdication and are often surprisingly funny. The queen mother was ever proper, but she also had a keen sense of mischief and liked a cocktail. (She founded the Windsor Wets' Club, a secret society of like-minded tipplers whose motto was *Aqua vitae non aqua pura*.) She promoted the benefits of fresh air, tea, homeopathy and a good joke. After the Italian invasion of Abyssinia in 1935, she wrote to the dying King George V: "Have you heard what the Abyssinian soldier said about Mussolini? 'He is my enema the Douche.'"

Why did Elizabeth succeed where Diana failed? She was less unstable, the media less intrusive and there were, in the king's phrase, "Us Two" in that marriage, rather than the three in Charles and Diana's. Readers will not learn anything new about what the two women thought of each other. One of Princess

Margaret's last acts, Mr Shawcross reveals, was to burn Diana's letters to her husband's grandmother. Such intriguing details make this book one of the few official biographies that is worth reading.

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Edward Kennedy's autobiography

A parting shot

Sep 17th 2009
From The Economist print edition

True Compass: A Memoir. By Edward Kennedy. *Twelve; 532 pages; $35. Little, Brown; £20*. Buy from Amazon.com, Amazon.co.uk

IT BEGINS with a death sentence. On May 20th 2008 Edward Kennedy woke from a "medicated drowsiness" in a Boston hospital to learn that he was about to die. Fortunately the cancer that was eating away at his brain spared him for long enough to see Barack Obama in the White House and to finish his memoirs. Rushed into publication just three weeks after his death, his autobiography is, at the time of writing, number two in the Amazon best-seller list in America, outsold only by Dan Brown's latest potboiler.

Alas, timing is not everything. Kennedy has an extraordinary story to tell. He was the last of nine children, three of whom went on to become senators and one of whom became president. At the age of seven he received his first holy communion from the pope in the Vatican. He became one of the most productive senators in American history, the author of some 2,500 major bills, at least 300 of which have become laws.

But "True Compass", though occasionally touching, is almost bereft of serious reflection. Kennedy saw the liberal dawn that was heralded by the New Frontier and the Great Society give way to a long conservative ascendancy. But he is happier demonising his opponents and delivering liberal bugle-calls than in analysing what went wrong, and what might go wrong again.

Kennedy tells us that when he was still a child his father once let him know that he had a choice between living "a serious life" and a "non-serious life". "I'll still love you whichever choice you make," his father, the bootlegger, wrote. "But if you decide to have a non-serious life, I won't have much time for you." Kennedy's inner life was a perpetual struggle between the serious and the non-serious. But he reveals much too little about the various scandals that defined his life, taking refuge, far too often, in the excuse that he needed to blot out intolerable memories. He writes even less about what it was like to live his life under the heavy burden of his father's expectations and his family's mystique.

Vermeer at the Met

A Dutch treat

Sep 17th 2009 | NEW YORK
From The Economist print edition

A chance to reassess a domestic masterpiece

Bridgeman



A woman with many admirers

FOUR hundred years ago a Dutch ship called the *Halve Maen* (Half Moon), Henry Hudson at the helm, arrived at the tiny island of Mannahatta. Less than half a century later Johannes Vermeer, a Delft artist, began painting scenes of the Dutch world Hudson left behind. On the anniversary of the voyage, the Rijksmuseum in Amsterdam has lent Vermeer's "The Milkmaid" to New York's Metropolitan Museum of Art, inspiring a modest show of paintings by Vermeer and other Dutch masters from the museum's collection. This is the first time this stunning painting has returned to America since New York hosted the World's Fair in 1939-40.

This may seem like an odd painting to mark the founding of *Niew Amsterdam*. "The Milkmaid" is not the most famous Dutch masterwork. Nor is it as strong a symbol of civic pride as Rembrandt's "Night Watch". Rather, it conjures up a quiet and dutiful domesticity. "What we have here is a maid who is treated in dignified and heroic terms," says Walter Liedtke, the Met's curator of European paintings, who organised this show.

Mr Liedtke calls this Vermeer's "last early work or the first mature work". The painter had no formal training. He began by borrowing widely from the masters before him, incorporating their influences (and often tempering their bawdiness) in his unparalleled compositions of stillness and repose. But "The Milkmaid", painted in 1657-58, features the glittering optics Vermeer ultimately became known for. He had a singular way of creating a mood with light and shadow, and he fills this painting with a glow from a window. It also reveals the technical expertise of the 25-year-old artist—his geometric modelling and vibrant colours. His works tend to "hypnotise the viewer regardless of what they know about the subject," says Mr Liedtke. There is a semi-voyeuristic relationship between viewers and this young woman.

The exhibition begins with copies of the 36 known Vermeer paintings, a reminder of his exclusivity. Vermeer had no manic fits of creativity, left no piles of preparatory sketches. He did not have a wealthy patron, and at the end of his life he could barely pay for bread. Each glowing moon-like face and vibrant folded cloth enjoys a rare value.

The crown prince of the Netherlands and his princess attended the show's opening. "It is seen as an act of diplomacy not just between the Rijksmuseum and the Met, but between the Netherlands and the United States," boasts Mr Liedtke. A bit of a stretch, but Vermeer's intimate rooms are a fine place for two countries to come together.

Economist.com PEOPLE OBITUARY

Norman Borlaug

Sep 17th 2009
From The Economist print edition

Norman Borlaug, feeder of the world, died on September 12th, aged 95

Corbis



AS DAWN broke over northern Mexico, Norman Borlaug wriggled from his sleeping bag. Rats had run over him all night, and he was cold. In a corner of the dilapidated research station where he had tried to sleep, he found a rusting plough. He took it outside, strapped the harness to himself, and began, furiously and crazily, in front of a group of astonished peasants, to plough the land.

The point was that he needed a tractor, and at once. He had come to Mexico in 1944, leaving a good job at DuPont, to increase grain yields, and to bring these half-starving people food. Hunger made its own imperatives. Feeding people could not wait. For the next ten years he was to work 12-hour days in these dry, baking fields, walking at a half-stoop to examine the stems for disease, perching on a stool to remove, with delicate tweezers, the male stamens of wheat flowers, harvesting wheat at one altitude to plant it immediately at another, until by 1956 Mexico's wheat production had doubled, and it had become self-sufficient.

Wherever he went, Mr Borlaug showed the same impatience. Paperwork was spurned in favour of action; planting, advising, training thousands. In India, where he set up hundreds of one-acre plots to show suspicious farmers how much they could grow, he was so frustrated by bureaucracy that when at last his seed came, shipped from Los Angeles, he planted it at once despite the outbreak of war between India and Pakistan, sometimes by flashes of artillery fire. And when in 1984 he was drawn out of semi-retirement to take his seed and techniques to Africa, he forgot in a moment, once he saw the place, his plan to do years of research first. "Let's just start growing," he said.

As a boy, he hadn't known what hunger was. He came from a small Norwegian farm in Iowa, the land of butter-sculptures and the breaded tenderloin sandwich. But on his first trip to "the big city", Minneapolis, in 1933, grown men had begged him for a nickel for a cup of coffee and a small, dry hamburger, and a riot had started round him when a milk-cart dumped its load in the street. He saw then how close to breakdown America was, because of hunger. It was impossible "to build a peaceful world on empty stomachs".

Crop diseases drew his attention first, inspiring him to turn from forestry to plant pathology under Charles

Stakman, a lifelong mentor, at the University of Minnesota. Rusts especially exercised him: how they lived, under the green live tissue of stems, how they spread, travelling for miles on the jet stream, and how they fell from the sky to infect even the healthiest crop, if the moisture and temperature were right. Rust had devastated the Midwest in the 1930s, and Mexico shortly before he went there. So Mr Borlaug first bred wheat cultivars for rust-resistance, a ten-year task, and then crossed them with Norin, a dwarf Japanese variety, to produce a shorter, straighter, stronger wheat which, when properly charged with water and fertiliser, gave three times the yield.

This was the wheat that swept India in its "Green Revolution", raising yields from 12m tonnes in 1965 to 20m by 1970, causing the country to run out of jute bags to carry it, carts and railcars to transport it, and places to store it; that made Pakistan self-sufficient in wheat by 1968; that almost doubled yields even in Sudan, on the edge of the Sahel. The famines and huge mortality that had been predicted for the second half of the 20th century never came to pass. More food led not to more births, but fewer, as the better-fed had smaller families. Global grain production outpaced population growth, and Mr Borlaug won the Nobel peace prize in 1970 for saving hundreds of millions of lives.

Greens attacked him, saying his new varieties used too much water and costly chemical fertiliser; his link with DuPont was noted. They complained that traditional farming was disrupted and diversity replaced by monoculture. Mr Borlaug called them naysayers and elitists, who had never known hunger but thought, for the health of the planet, that the poor should go without good food. Higher yields, he pointed out, saved marginal land and forest from farming. Inorganic fertiliser just replaced natural nutrients, and more efficiently than manure. As for cross-breeding, Mother Nature had done it first, cross-pollinating different wild grasses until they produced a grain that could eventually expand into modern bread.

The ticking clock

Genetic engineering of plants greatly excited him. The risks, he said, were rubbish, unproven by science, while the potential benefits were endless. The transfer of useful characteristics might now take weeks, rather than decades. More lives would be saved. The gene for rust-resistance in rice, for example, might be put into all other cereals. He hoped he might live to see it.

Meanwhile what he called the "Population Monster" was breathing down his neck, or rather ticking, like Captain Hook's crocodile. Every second brought two more people, crying to be fed. By 2050, he wrote in 2005, the world would need to double its food supply. Some 800m were malnourished as it was. Mr Borlaug loved to talk of reaching for the stars, but his day-to-day motto was an earthly one. Get the plough. Start growing now.



Overview

Sep 17th 2009
From The Economist print edition

Consumer prices in **America** rose by 0.4% in August but were 1.5% lower than they were a year earlier. Much of the monthly rise was the result of a jump in petrol prices. The value of retail sales surged by 2.7% in August, caused largely by a sharp increase in car sales, as consumers took advantage of government cash incentives. Stronger output by carmakers helped boost industrial production, which rose by 0.8% in the month.

America's **current-account deficit** narrowed from $104.5 billion to $98.8 billion (or 2.8% of GDP) in the second quarter.

Inflation in the **euro area** fell by 0.2% in the year to August, unrevised from a provisional estimate. Finland has the highest harmonised inflation rate in the currency zone, at 1.3%. At the other extreme, prices in Ireland were 2.4% lower than a year earlier.

The rate of consumer-price inflation in **Britain** fell from 1.8% to 1.6% in August. The unemployment rate rose to 7.9% in the three months to July.

Sweden's GDP rose by 0.2% in the second quarter, revised up from an earlier estimate.

Brazil's GDP rose by 1.9% in the three months to the end of June but was 1.2% lower than in the same quarter in 2008.

Industrial production in **Mexico** fell by 6.5% in the year to July. **India**'s output in July edged further down from its recent peak in March but was nevertheless 7% higher than in July 2008.



Output, prices and jobs

Sep 17th 2009
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Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2009†	2010†	latest	latest	year ago	2009†	rate‡, %
United States	−3.9 Q2	−1.0	−2.6	+2.5	−10.7 Aug	−1.5 Aug	+5.4	−0.4	9.7 Aug
Japan	−6.4 Q2	+3.7	−5.5	+1.4	−22.7 Jul	−2.2 Jul	+2.3	−1.1	5.7 Jul
China	+7.9 Q2	na	+8.1	+8.5	+12.3 Aug	−1.2 Aug	+4.9	−0.8	9.0 2008
Britain	−5.5 Q2	−2.6	−4.3	+1.1	−9.3 Jul	+1.6 Aug§	+4.7	+1.7	7.9 Jul††
Canada	−3.2 Q2	−3.4	−2.2	+2.1	−12.7 Jun	−0.9 Jul	+3.4	+0.6	8.7 Aug
Euro area	−4.7 Q2	−0.5	−3.9	+1.2	−15.9 Jul	−0.2 Aug	+3.8	+0.4	9.5 Jul
Austria	−4.4 Q2	−1.7	−2.9	+0.6	−11.4 Jun	+0.3 Aug	+3.7	+0.4	4.4 Jul
Belgium	−3.7 Q2	−1.1	−3.3	+0.7	−13.4 Jun	−0.8 Aug	+5.4	+0.3	12.3 Jul‡‡
France	−2.6 Q2	+1.4	−2.1	+1.5	−13.0 Jul	−0.2 Aug	+3.2	+0.2	9.8 Jul
Germany	−5.9 Q2	+1.3	−5.0	+1.6	−16.9 Jul	nil Aug	+3.1	+0.2	8.3 Aug
Greece	−0.3 Q2	+1.0	−3.5	−0.8	−9.2 Jul	+0.8 Aug	+4.7	+0.5	8.6 Jun
Italy	−6.0 Q2	−1.9	−4.9	+0.7	−18.2 Jul	+0.1 Aug	+4.1	+0.8	7.3 Q1
Netherlands	−5.1 Q2	−3.4	−4.1	+1.0	−12.7 Jun	+0.3 Aug	+3.2	+1.3	5.0 Aug††
Spain	−4.2 Q2	−4.2	−3.8	−0.5	−16.7 Jul	−0.8 Aug	+4.9	−0.3	18.5 Jul
Czech Republic	−4.9 Q2	+1.2	−3.5	+1.2	−18.2 Jul	+0.2 Aug	+6.5	+1.1	8.5 Aug
Denmark	−4.1 Q1	−4.2	−3.8	+0.7	−14.3 Jul	+1.1 Aug	+4.3	+1.1	3.7 Jul
Hungary	−7.6 Q2	−8.1	−6.3	−1.0	−19.4 Jul	+5.0 Aug	+6.5	+4.3	9.7 Jul††
Norway	−4.8 Q2	−5.0	−2.0	+0.5	−8.0 Jul	+1.9 Aug	+4.5	+2.5	3.0 Jun§§
Poland	+1.1 Q2	na	+0.7	+1.5	−4.6 Jul	+3.7 Aug	+4.8	+3.3	10.8 Jul‡‡
Russia	−10.9 Q2	na	−7.0	+2.5	−12.6 Aug	+11.6 Aug	+15.0	+12.1	8.3 Jul‡‡
Sweden	−6.0 Q2	+0.6	−4.8	+1.7	−19.9 Jul	−0.8 Aug	+4.3	−0.2	8.0 Aug‡‡
Switzerland	−2.0 Q2	−1.0	−2.1	+0.7	−14.0 Q2	−0.8 Aug	+2.9	−0.5	4.0 Aug
Turkey	−7.0 Q2	na	−5.4	+2.7	−9.2 Jul	+5.3 Aug	+11.8	+6.1	13.6 May‡‡
Australia	+0.6 Q2	+2.5	+0.5	+2.0	−3.8 Q2	+1.5 Q2	+4.5	+1.6	5.8 Aug
Hong Kong	−3.8 Q2	+13.9	−3.3	+2.8	−9.5 Q2	−1.5 Jul	+6.3	−0.3	5.4 Jul††
India	+6.1 Q2	na	+5.5	+6.3	+7.0 Jul	+11.9 Jul	+8.3	+7.7	6.8 2008
Indonesia	+4.0 Q2	na	+4.1	+4.4	+0.2 Jun	+2.8 Aug	+11.8	+4.4	8.1 Feb
Malaysia	−3.9 Q2	na	−3.0	+3.6	−8.4 Jul	−2.4 Aug	+8.5	−0.1	4.0 Q1
Pakistan	+2.0 2009**	na	+3.7	+2.7	−4.4 Jun	+10.7 Aug	+25.3	+13.0	5.2 2008
Singapore	−3.5 Q2	+20.7	−6.0	+3.6	+12.4 Jul	−0.5 Jul	+6.5	−0.2	3.3 Q2
South Korea	−2.5 Q2	+9.7	−1.6	+2.1	+0.7 Jul	+2.2 Aug	+5.6	+2.7	3.8 Aug
Taiwan	−7.5 Q2	na	−3.6	+3.5	−8.1 Jul	−0.8 Aug	+4.7	−1.1	6.0 Jul
Thailand	−4.9 Q2	+9.6	−4.3	+3.3	−7.3 Jul	−1.0 Aug	+6.5	−1.0	2.4 May
Argentina	+2.0 Q1	+0.2	−3.5	+0.5	−9.0 Jul	+5.9 Aug	+9.0	+6.2	8.8 Q2‡‡
Brazil	−1.2 Q2	+7.8	−1.0	+3.3	−9.9 Jul	+4.4 Aug	+6.2	+4.8	8.0 Jul‡‡
Chile	−4.5 Q2	−1.4	−1.2	+3.0	−7.4 Jul	−1.0 Aug	+9.3	+1.9	10.8 Jul††‡‡
Colombia	−0.6 Q1	+0.9	−1.0	+2.5	−6.6 Jun	+3.1 Aug	+7.9	+4.6	12.6 Jul‡‡
Mexico	−10.3 Q2	−4.4	−7.1	+2.8	−6.5 Jul	+5.1 Aug	+5.6	+5.4	6.1 Jul‡‡
Venezuela	−2.4 Q2	na	−3.0	−3.4	−12.4 Jun	+28.8 Aug	+34.5	+27.2	7.7 Q2‡‡
Egypt	+4.2 Q1	na	+4.5	+3.9	+5.8 Q1	+9.0 Aug	+23.7	+9.8	9.4 Q2‡‡
Israel	+0.1 Q2	+1.0	−1.1	+1.5	−8.6 Jun	+3.1 Aug	+5.0	+3.1	8.0 Q2
Saudi Arabia	+4.5 2008	na	−1.0	+3.3	na	+4.1 Aug	+10.9	+4.3	na
South Africa	−2.8 Q2	−3.0	−2.2	+3.1	−13.7 Jul	+6.7 Jul	+13.4	+7.1	23.6 Jun‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	−16.1 Q2	na	−13.0	−3.0	−27.8 Jul	−0.9 Aug	+11.0	−0.8	17.0 Jun
Finland	−8.9 Q2	−10.0	−5.4	+0.4	−24.0 Jul	−0.7 Aug	+4.7	nil	8.9 Jul
Iceland	−6.5 Q2	−7.8	−6.2	+0.5	+10.1 2008	+10.9 Aug	+14.5	+12.0	8.0 Jul‡‡
Ireland	−8.5 Q1	−5.7	−7.7	−2.5	+2.6 Jun	−5.9 Jul	+4.4	−3.6	12.2 Jul
Latvia	−18.7 Q2	na	−17.0	−4.0	−17.7 Jul	+1.8 Aug	+15.7	+3.3	17.2 Jun
Lithuania	−22.4 Q2	−40.8	−15.0	−4.5	−15.7 Jul	+2.6 Aug	+11.9	+4.6	9.7 Jul‡‡
Luxembourg	−5.5 Q1	−5.9	−4.5	−0.8	−14.7 Jun	−0.7 Jul	+4.9	+0.5	5.5 Jul‡‡
New Zealand	−2.2 Q1	−2.7	−2.1	+1.2	−11.4 Q1	+1.9 Q2	+4.0	+1.8	6.0 Q2
Peru	−2.1 Jun	na	+1.3	+2.7	−12.2 Jun	+1.9 Aug	+6.3	+3.5	7.9 Jul‡‡
Philippines	+1.2 Q2	+9.8	+1.5	+3.8	−10.8 Jun	+0.1 Aug	+12.4	+2.9	7.6 Q3‡‡
Portugal	−3.7 Q2	+1.4	−4.1	−0.4	−9.0 Jul	−1.5 Jul	+3.1	−0.7	9.1 Q2‡‡
Slovakia	−5.3 Q2	na	−5.5	+1.0	−21.6 Jul	+1.3 Aug	+5.0	+2.1	12.1 Jul‡‡
Slovenia	−9.3 Q2	na	−7.0	nil	−22.3 Jun	nil Aug	+6.0	+0.8	9.1 Jun‡‡
Ukraine	−20.3 Q1	na	−17.0	+1.0	−26.7 Jul	+15.3 Aug	+26.0	+16.0	2.2 Jul
Vietnam	+4.5 Q2	na	+4.2	+4.8	+5.6 Aug	+2.0 Aug	+28.3	+6.8	4.6 2007

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions. §RPI inflation rate -1.3 in August. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. §§Centred 3-month average

Sources: National statistics offices and central banks; Thomson Reuters; Centre for Monitoring Indian Economy; OECD; ECB

The Economist commodity-price index

Sep 17th 2009
From The Economist print edition

***The Economist* commodity-price index**
2000=100

	Sep 8th	Sep 15th*	% change on one month	% change on one year
Dollar index				
All items	193.1	190.4	+0.3	-13.4
Food	194.6	196.7	+2.0	-12.0
Industrials				
All	191.2	182.1	-2.0	-15.1
Nfa†	148.0	144.3	+0.9	-18.6
Metals	214.9	202.8	-3.1	-13.7
Sterling index				
All items	176.8	175.7	+0.9	-6.4
Euro index				
All items	123.0	120.6	-3.1	-16.2
Gold				
$ per oz	995.85	1001.00	+7.0	+28.8
West Texas Intermediate				
$ per barrel	71.22	70.87	+2.4	-24.0

*Provisional †Non-food agriculturals.

Economic freedom

Sep 17th 2009
From The Economist print edition



Hong Kong tops an annual index from the Fraser Institute, a Canadian think-tank, which ranks 141 countries according to the degree to which their policies support economic freedom. Countries that promote trade (both internal and external), free competition and strong legal protection for private property score well. America comes sixth in the survey, just behind Chile but ahead of the big continental European countries. Germany is ranked one place above Japan, the other main export-led economy in the rich world. The big emerging economies do fairly poorly. China is just above Russia in 82nd place. Brazil is outside the top 100. Zimbabwe has the dubious distinction of coming bottom of the think-tank's list.



Trade, exchange rates, budget balances and interest rates

Sep 17th 2009
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2009†	Currency units, per $ Sep 16th	Currency units, per $ year ago	Budget balance % of GDP 2009†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−604.9 Jul	−542.3 Q2	−2.9	–	–	−13.5	0.20	3.47
Japan	+10.8 Jul	+114.0 Jul	+2.7	91.1	105	−7.4	0.39	1.30
China	+267.0 Aug	+364.4 Q2	+6.1	6.83	6.84	−4.2	1.75	3.64
Britain	−135.2 Jul	−52.5 Q1	−1.8	0.61	0.56	−14.4	0.62	3.79
Canada	+9.5 Jul	−19.1 Q2	−2.1	1.07	1.08	−2.4	0.22	3.37
Euro area	−40.1 Jun	−157.5 Jun	−0.9	0.68	0.70	−6.5	0.77	3.32
Austria	−5.5 Jun	+10.7 Q1	+1.3	0.68	0.70	−5.6	0.77	3.70
Belgium	+8.0 Jul	−11.8 Mar	−2.2	0.68	0.70	−5.9	0.78	3.71
France	−65.3 Jul	−54.0 Jul	−2.2	0.68	0.70	−8.2	0.77	3.58
Germany	+179.4 Jul	+158.0 Jul	+4.0	0.68	0.70	−4.7	0.77	3.33
Greece	−50.6 Jun	−41.6 Jun	−8.5	0.68	0.70	−6.8	0.77	4.52
Italy	−11.2 Jun	−62.8 Jun	−2.5	0.68	0.70	−5.3	0.77	4.05
Netherlands	+44.3 Jul	+50.0 Q1	+6.2	0.68	0.70	−4.0	0.77	3.58
Spain	−92.5 Jun	−109.6 Jun	−6.7	0.68	0.70	−10.6	0.77	3.83
Czech Republic	+4.4 Jul	−5.2 Jul	−1.5	17.1	17.0	−4.8	1.89	5.05
Denmark	+8.2 Jul	+8.8 Jul	+0.9	5.07	5.26	−2.5	1.77	3.70
Hungary	+3.3 Jul	−11.3 Q1	−2.9	184	172	−4.3	7.92	7.89
Norway	+53.9 Aug	+69.5 Q2	+14.6	5.86	5.89	7.1	1.89	4.19
Poland	−11.7 Jul	−11.0 Jul	−0.5	2.82	2.37	−3.7	4.20	6.05
Russia	+112.5 Jul	+55.3 Q2	+1.9	30.6	25.6	−8.0	10.50	10.74
Sweden	+12.9 Jul	+29.0 Q2	+6.8	6.90	6.79	−4.4	0.18	3.37
Switzerland	+15.8 Jul	+56.6 Q1	+6.8	1.03	1.12	−1.3	0.30	2.12
Turkey	−42.9 Jul	−16.2 Jul	−0.6	1.48	1.28	−5.5	8.09	5.73‡
Australia	+5.3 Jul	−29.0 Q2	−4.0	1.15	1.27	−3.8	3.36	5.26
Hong Kong	−21.0 Jul	+29.6 Q1	+11.4	7.75	7.78	−3.8	0.22	2.24
India	−87.4 Jul	−29.8 Q1	−1.1	48.2	46.3	−8.0	3.39	7.64
Indonesia	+12.5 Jul	+4.4 Q2	+1.2	9,720	9,400	−2.8	6.98	5.86‡
Malaysia	+35.9 Jul	+40.5 Q1	+14.8	3.48	3.45	−8.0	2.14	2.22‡
Pakistan	−15.5 Aug	−8.9 Q2	−3.2	82.8	77.2	−4.3	12.60	9.85‡
Singapore	+18.6 Aug	+21.4 Q2	+13.8	1.41	1.43	−3.2	0.50	2.27
South Korea	+26.3 Aug	+27.6 Jul	+3.9	1,211	1,116	−4.5	2.60	5.27
Taiwan	+18.0 Aug	+31.9 Q2	+9.6	32.5	32.1	−5.0	0.85	1.33
Thailand	+11.3 Jul	+9.0 Jul	+5.5	33.7	34.4	−5.8	1.35	3.26
Argentina	+17.5 Jul	+6.8 Q1	+3.4	3.83	3.10	−0.9	13.75	na
Brazil	+27.8 Aug	−17.9 Jul	−1.3	1.80	1.86	−2.6	8.65	6.16‡
Chile	+6.0 Aug	−3.6 Q2	−0.9	545	546	−4.0	0.60	1.85‡
Colombia	−0.8 Jul	−6.5 Q1	−3.3	1,955	2,132	−3.0	4.99	5.28‡
Mexico	−16.0 Jul	−14.0 Q2	−2.4	13.2	10.9	−4.0	4.49	7.93
Venezuela	+18.5 Q2	+10.3 Q2	+0.7	5.63§	4.88§	−7.6	14.51	6.55‡
Egypt	−26.1 Q1	−2.9 Q1	−2.1	5.51	5.48	−6.9	9.62	2.65‡
Israel	−8.0 Aug	+5.6 Q2	+1.7	3.75	3.53	−5.7	0.80	3.85
Saudi Arabia	+212.0 2008	+134.0 2008	+5.6	3.75	3.75	−0.3	0.65	na
South Africa	−3.6 Jul	−15.8 Q2	−5.3	7.34	8.20	−4.5	6.98	8.55
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−1.9 Jul	−0.1 Jul	+0.7	10.7	11.0	−4.0	5.58	na
Finland	+5.5 Jul	+4.3 Jul	+0.6	0.68	0.70	−2.8	0.75	3.60
Iceland	+0.8 Aug	−4.5 Q2	−5.3	124	94.7	−13.1	8.29	na
Ireland	+49.8 Jun	−11.3 Q1	−2.7	0.68	0.70	−13.0	0.77	4.75
Latvia	−3.3 Jul	−0.1 Jul	+2.5	0.48	0.50	−11.0	9.61	na
Lithuania	−3.9 Jun	−0.9 Jul	+1.3	2.35	2.43	−7.0	6.88	na
Luxembourg	−6.9 Jun	+2.2 Q1	na	0.68	0.70	−4.0	0.77	na
New Zealand	−2.1 Jul	−11.8 Q1	−7.7	1.41	1.52	−6.8	3.70	5.89
Peru	+2.5 Jul	−2.1 Q2	−2.3	2.90	2.98	−2.3	1.25	na
Philippines	−6.8 Jun	+5.1 Mar	+4.4	48.0	47.1	−3.6	4.25	na
Portugal	−27.5 Jul	−24.2 Jun	−8.8	0.68	0.70	−7.4	0.77	3.90
Slovakia	−0.2 Jul	−4.3 Jun	−4.0	20.5	21.3	−5.5	1.35	3.89
Slovenia	−2.5 Jul	−1.9 Jun	−1.2	0.68	0.70	−5.9	0.77	na
Ukraine	−13.4 Q1	−6.5 Q2	−0.5	8.53	4.95	−7.0	14.75	na
Vietnam	−6.6 Aug	−7.0 2007	−6.9	17,833	16,610	−9.0	8.69	6.29

*Merchandise trade only. †The Economist poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.



Markets

Sep 17th 2009
From The Economist print edition

Markets

	Index Sep 16th	% change on one week	% change on Dec 31st 2008 in local currency	% change on Dec 31st 2008 in $ terms
United States (DJIA)	9,791.7	+2.6	+11.6	+11.6
United States (S&P 500)	1,068.8	+3.4	+18.3	+18.3
United States (NAScomp)	2,133.2	+3.5	+35.3	+35.3
Japan (Nikkei 225)	10,270.8	−0.4	+15.9	+15.4
Japan (Topix)	931.4	−0.9	+8.4	+7.9
China (SSEA)	3,148.2	+1.8	+64.7	+64.6
China (SSEB, $ terms)	203.9	+1.7	+83.9	+83.9
Britain (FTSE 100)	5,124.1	+2.4	+15.6	+32.6
Canada (S&P TSX)	11,555.6	+5.0	+28.6	+48.4
Euro area (FTSE Euro 100)	891.6	+2.4	+19.5	+26.2
Euro area (DJ STOXX 50)	2,882.3	+2.2	+17.8	+24.4
Austria (ATX)	2,582.6	+2.2	+47.5	+55.9
Belgium (Bel 20)	2,500.2	+2.2	+31.0	+38.4
France (CAC 40)	3,813.8	+2.9	+18.5	+25.2
Germany (DAX)*	5,700.3	+2.3	+18.5	+25.2
Greece (Athex Comp)	2,550.1	+0.6	+42.7	+50.8
Italy (FTSE/MIB)	23,465.5	+2.9	+20.6	+27.4
Netherlands (AEX)	312.8	+2.8	+27.2	+34.4
Spain (Madrid SE)	1,228.0	+2.3	+25.8	+33.0
Czech Republic (PX)	1,154.8	+0.2	+34.6	+51.7
Denmark (OMXCB)	319.2	+0.8	+41.1	+49.1
Hungary (BUX)	20,217.5	+6.3	+65.2	+71.7
Norway (OSEAX)	371.7	+2.9	+37.6	+64.5
Poland (WIG)	36,635.0	−2.4	+34.5	+41.6
Russia (RTS, $ terms)	1,246.8	+7.5	+97.6	+97.3
Sweden (OMXS30)†	918.4	−0.3	+38.7	+59.0
Switzerland (SMI)	6,299.9	+1.6	+13.8	+17.2
Turkey (ISE)	46,680.7	+4.7	+73.8	+81.7
Australia (All Ord.)	4,652.8	+2.8	+27.2	+55.7
Hong Kong (Hang Seng)	21,402.9	+2.6	+48.8	+48.8
India (BSE)	16,677.0	+3.0	+72.9	+74.6
Indonesia (JSX)	2,439.4	+2.4	+80.0	+101.8
Malaysia (KLSE)	1,213.0	+1.4	+38.3	+37.5
Pakistan (KSE)	9,137.1	+0.6	+55.8	+48.9
Singapore (STI)	2,674.4	+0.9	+51.8	+54.8
South Korea (KOSPI)	1,683.3	+4.7	+49.7	+55.7
Taiwan (TWI)	7,440.2	+2.6	+62.1	+63.8
Thailand (SET)	710.3	+2.1	+57.8	+62.8
Argentina (MERV)	1,977.4	+5.5	+83.2	+65.3
Brazil (BVSP)	60,410.0	+4.3	+60.9	+108.4
Chile (IGPA)	15,437.4	+1.7	+36.3	+59.3
Colombia (IGBC)	10,808.9	+1.7	+43.0	+64.4
Mexico (IPC)	29,625.0	+1.8	+32.4	+39.0
Venezuela (IBC)	53,550.5	+1.6	+52.6	+64.3
Egypt (Case 30)	6,723.3	+1.0	+46.3	+46.4
Israel (TA-100)	907.2	+0.3	+60.8	+61.9
Saudi Arabia (Tadawul)	5,713.0	+1.7	+18.9	+19.0
South Africa (JSE AS)	25,578.8	+2.0	+18.9	+49.7
Europe (FTSEurofirst 300)	1,006.2	+1.9	+20.9	+27.8
World, dev'd (MSCI)	1,138.3	+2.9	+23.7	+23.7
Emerging markets (MSCI)	913.5	+3.8	+61.1	+61.1
World, all (MSCI)	289.7	+3.0	+27.3	+27.3
World bonds (Citigroup)	841.3	+0.8	+3.9	+3.9
EMBI+ (JPMorgan)	484.7	+3.0	+23.8	+23.8
Hedge funds (HFRX)§	1,123.8	+0.5	+10.1	+10.1
Volatility, US (VIX)	23.7	24.3	40.0	(levels)
CDSs, Eur (iTRAXX)‡	95.4	−9.3	−52.8	−50.1
CDSs, N Am (CDX)‡	141.7	−17.9	−39.3	−39.3
Carbon trading (EU ETS) €	14.1	−6.8	−12.3	−7.3

*Total return index. †New series. ‡Credit-default swap spreads, basis points. Sources: National statistics offices, central banks and stock exchanges; Thomson Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac. §Sep 15th

Foreign direct investment

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Foreign direct investment (FDI)—the purchase of factories, buildings and other assets by foreign firms—has fallen sharply since the start of the financial crisis, according to the latest World Investment Report from UNCTAD. FDI in rich countries has been hardest hit. At its recent peak in the last quarter of 2007, 80% of the world's FDI went to developed economies. By the first quarter of this year FDI into rich countries was less than two-thirds of the total. FDI to emerging economies has held up better. Flows to Africa rose to a new record of $88 billion last year, much of it going to countries rich in natural resources. Foreign investment in China and India also surged, as companies sought footholds in resilient economies.